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European Tax Survey

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TAXATION PAPERS

EUROPEAN TAX SURVEY

Working paper n°3 October 2004

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EXECUTIVE SUMMARY

The European Tax Survey

In order to have a better understanding of the impact of taxation on companies' decisions and activities, and potential costs that may arise from the lack of coordination in this area at EU level, the European Commission's Taxation and Customs Union Directorate-General launched a European Tax Survey. Seven hundred companies active in the EU participated in the Survey providing information on a large number of tax compliance related issues. Company responses included quantitative estimates of their compliance costs and opinions on a number of issues related to tax systems.

Companies from all the then EU-15 countries had the opportunity to participate in the survey and the 700 companies that participated cover 14 EU Member States.¹ In order to correct for under- or over-representation of some countries the responses of companies were weighted in order to reflect the number of companies of the same size in their country. However, due to the relatively low number of responses, the results presented below do not pretend to provide a fully representative picture of the EU, as is explained in Chapter 1. This does not preclude, however, drawing interesting and innovative insights from the considerable amount of information provided by the 700 companies involved in the survey.

The European Tax Survey contained both quantitative and qualitative questions, which are analyzed in turn.

Main results of the quantitative analysis

The first part of the study bears on a quantitative analysis of data concerning the perceived total absolute compliance costs of companies (Chapter 2). These compliance costs consist of company taxation and Value Added Taxation (VAT) compliance costs in the EU and company taxation compliance costs outside the EU. The first stage of this quantitative analysis presents the weighted perceived compliance costs of the EU companies. The second stage presents a series of regression analyses.

Compliance costs relative to sales are larger for SMEs than for large companies

The data provided by companies on their perceived compliance costs, taxes paid and sales leads to the following main results:

- Weighted total absolute compliance costs are estimated at €1.460.000 for large companies. This corresponds to 1.9% of taxes paid and to 0.02% of sales, respectively. The figures for large companies are consistent with figures presented in other studies.
- Weighted total absolute compliance costs are estimated at €203.000 for Small and Medium-sized Enterprises (SMEs). This amount corresponds to 30.9% of taxes paid and to

¹ No companies from Luxembourg participated in the survey. For most of the topics, information for France was not available.

2.6% of sales, respectively. However, these ratios should be taken with great caution for reasons explained in Section 2.2.

- Econometric regressions provided significant and recurrent evidence that total, VAT and company taxation compliance costs increase with company size and impose a higher relative burden on smaller companies. These results are in line with established findings in the economic literature.

Cross-border activity leads to higher compliance costs for companies

Furthermore, the econometric analysis provides a strong body of evidence as to the importance of cross-border activities for compliance costs and highlights some of the variables that are correlated with compliance costs:

- Compliance costs are higher for companies with at least one subsidiary in another EU Member State compared with companies without subsidiaries in another Member State.
- Compliance costs increase with the number of subsidiaries abroad.

In the context of a study focusing on the impact of taxation on the functioning of the Internal market, these results need to be particularly stressed. The econometric results based on the data provided by the 700 EU companies participating in the European Tax Survey provided quantitative evidence that there is an additional cost for companies that are active cross border in the EU. Significant results in this respect recurred in the various estimated models.

Main results of the qualitative analysis

The quantitative analysis was complemented by a qualitative analysis. The latter aimed to provide better information on the sample companies' opinions on a number of tax related issues and to facilitate the interpretation of the quantitative results.

Transfer pricing requirements are a major difficulty in the company tax area

Companies participating in the European Tax Survey were asked to indicate whether a number of tax requirements lead to difficulties. The analysis of their responses related to company taxation shows the following:

- Tax accounting and record keeping requirements as well as audits and litigations are the issues related to company taxation which raise the main concerns in the domestic context;
- In relation to foreign-sourced income, the results highlight that large companies with a branch, a subsidiary or a permanent establishment in another EU Member State have particular difficulties with regard to audits and litigations. Furthermore, transfer pricing appears as a major tax obstacle. The estimates highlight that transfer pricing is an important issue for 82.8% of large companies, in particular when it comes to dealing with documentation requirements, which are a difficulty for 81.9% of the large companies.

Repayment and refund requirements are a major difficulty in the VAT area

Companies participating in the European Tax Survey were also asked to provide their opinion on a number of tax requirements related to VAT in the domestic and foreign context. The main findings are as follows:

- Four issues raise particular difficulties for companies in the domestic context, namely audits and litigations, record keeping requirements, the complexity of tax returns and listings and invoicing requirements.
- In relation to VAT obligations in other Member States, one issue appears particularly problematic for large companies, namely the repayment and refund requirements. Other issues, such as accessing tax information and contacting tax officials and audits and litigations appear also to lead to difficulties.
- The difficulty of repayment and refund requirements in other EU Member States is especially prominent for companies registered in a Member State where they do not have a permanent establishment. It is estimated that 86.1% of large companies incurring VAT costs on their inputs in an EU Member State without being registered have difficulties coping with procedures for refunds under the 8th VAT directive. In fact, the complexity or the length of the procedure are such that an estimated 53.5% of large companies have not requested refunding at some point. The estimates furthermore indicate that 14.2% of small and 9.9% of large companies have not carried out VAT taxable activities in another Member State where they do not have a permanent establishment because of VAT compliance requirements.

Taxation is a factor for investment location decisions

In addition to questions related to tax requirements, participants in the European Tax Survey were also asked a number of questions on the impact of taxation on decisions relating to investment and company structure. The results suggest that taxation could affect the choice of location and the type of investment in the EU. In particular,

- The results highlight that taxation is a relevant factor mainly for the location of production plants, coordination centres and financial services centres;
- When it comes to mergers and acquisitions, taxation could also prove to be a serious issue. The estimates show that a majority of firms that merged with, or acquired another business in the EU during the past five years had difficulties regarding capital gain taxes and double taxation.

Taxation affects company structure decisions

The analysis also shows that tax conditions affect companies' decisions concerning the financial and legal structure of their international operations. The main findings here are:

- For 87.3% of the companies taxes can influence decisions on whether foreign operations should be organised through a subsidiary, a branch or a permanent establishment;

- Estimates indicate that 77.2% of the companies consider tax as a factor when they decide to use new equity or debt when financing foreign operations directly or indirectly via the parent company;
- Overall, companies with cross-border activities are significantly more sensitive to taxation when deciding the financial and legal structure of their operations than those who are active only in one country.

Conclusions

This study highlights the importance of taxation for a very broad range of operations of companies in the Internal market. The evidence obtained from the responses provided by the 700 companies involved in the European Tax Survey strongly indicates that compliance costs of EU companies increase when they undertake cross-border activities in the EU. These costs also increase when company activities increase, for example by setting up new subsidiaries in other EU Member States, *ceteris paribus*.

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1. INTRODUCTION

1.1. Context

In its Communication of May 2001 on "Tax policy in the European Union - Priorities for the years ahead" [COM(2001) 260], the European Commission stressed that the Community should "put the main addressees of the Internal Market - its citizens and enterprises - centre-stage". In this perspective, and with a view to facilitating a smooth functioning of the Internal market, it indicated the necessity for EU tax systems to be sufficiently flexible and responsive in order to keep pace with international developments, whilst remaining as simple as possible in order to minimise compliance costs. The same Communication indicated that EU tax policy should, as a priority, serve the interests of citizens and business wishing to avail themselves of the four freedoms of the Internal Market (the free movement of persons, goods and capital, and the freedom to provide services). It should, therefore, "focus on the removal of tax obstacles to the exercise of those four freedoms". In fact, it added, "eight years after the target date for completion of the Internal Market, it is unacceptable that many obstacles remain to the attainment of key Community objectives. (...) increased attention must be paid to the removal of these obstacles. It is high time to put much more emphasis on the concerns of the EU taxpayer".

Since the 2001 Communication, several breakthroughs have occurred in the field of taxation. In the indirect tax area, the new VAT strategy has led to significant changes to existing legislation or new rules, e.g. in relation to electronic commerce and invoicing. Furthermore, a new directive on energy taxation has entered into force at the beginning of 2004. In the direct tax area, the agreement on the tax package should lead to significant changes, in particular with regard to savings taxation. Yet, despite these positive developments, much remains to be done to eliminate tax obstacles and facilitate the life of taxpayers active in the Internal Market. This was confirmed in the Communication of 2003 "An Internal Market without company tax obstacles achievements, ongoing initiatives and remaining challenges" [COM(2003)726], which indicated that the tax obstacles identified by the Commission in 2001 are still highly relevant. "In particular, the need for companies to deal with 15 and soon 25 or more different tax systems clearly remains the ultimate cause of most of the tax problems within the Internal Market and of high compliance costs."

In this context, and with an aim to contributing to the tax debate in the EU and obtaining a clearer idea of remaining issues linked to the functioning of the Internal market, as well as facilitating future work on those issues, it was considered useful to produce further evidence of the existence and the causes of tax obstacles and compliance costs in the Internal Market. The Commission services therefore launched the European Tax Survey, whose main findings are contained in the present Commission Staff Working Paper.

1.2. Objectives of the study

The study presented here is based on the responses obtained from a survey, the European Tax Survey, sent to more than 2000 EU companies by the Commission in September 2003 (see Box 1-1). There were two main objectives for this survey. Firstly, it aimed at gaining a better understanding of how the need to cope with 15 separate tax

systems impacts on companies, in particular on their compliance costs and their decision making². The second objective of the survey was to try and quantify the compliance costs of EU companies and to examine how they differ with regard to company sizes and sectors. The launch of the European Tax Survey would also constitute a unique opportunity to collect a great deal of useful information on both company taxation and VAT which could lead to a detailed analysis of current issues affecting companies.

Box 1-1 The European Tax Survey

The European Tax Survey was launched on the 1st of September 2003 and closed on the 31st of January 2004. In order to take part to this survey companies needed to register as a member of the European Business Test Panel (EBTP) set up by the Commission's Internal Market Directorate-general (<http://europa.eu.int/yourvoice/ebtp/>). The EBTP has been introduced to provide companies the possibility to express their view on new legislative proposals and policy initiatives under consideration by the Commission.

Both registration for the EBTP and participation in the European Tax Survey are entirely Internet based. Membership of the EBTP is free of charge and requires on-line registration which involves the provision of some basic characteristics on the company represented by the respondent. Companies that register for the EBTP do this on a voluntary basis. Registered companies do not have the obligation to participate in any survey. However, it is expected that registered companies participate in most surveys. The survey was available in all the then eleven official languages of the EU.

It is useful to note that companies taking part in the EBTP do not know beforehand the specific topic that will be dealt with. Participants to the panel did not receive prior information on the fact that a tax survey would be launched. This is important, because it limits risks of a strong bias in the selection procedure of participating companies compared to a one-shot survey aimed specifically at tax issues.

Furthermore, the EBTP aims at providing a representative picture of the views of EU companies and reflect the importance of company size and sector in the European Union. Therefore, it is constructed in order to obtain a target sample of 2992 companies over countries, company size groups and sectors, which would be representative of the EU economy (Annex B provides information on operational aspects of the European Business Test Panel).

As announced in the Communication on tax obstacles of 24 November 2003 [COM(2003)726] the results of the survey should also give a general indication of whether, and if so the extent to which, companies do feel it is more difficult to comply with the administrative aspects of company and VAT once they become active cross-border. Moreover, the results should indicate the extent to which the difficulties associated with transfer pricing and mergers and acquisitions are seen as obstacles to cross-border activities in the EU. Lastly, they should indicate the extent to which, if at

² The survey was launched and concluded before the EU enlargement of 1st May 2004. Companies operating in the 10 new Member States are therefore not covered by the European Tax Survey.

all, company taxation issues influence companies' decisions as regards their corporate and financing structures – which could of course lead to sub-optimal decisions for the economy as a whole.

In practice, all the aforementioned topics are examined in the following chapters. The specific content of the chapters, their relation and the overall structure of the study are explained below.

1.3. Methodology and limitations of the study

1.3.1. A small sample of companies

As explained in Box 1-1 above, the European Tax Survey is based on responses provided by participants to the European Business Test Panel (EBTP). The EBTP ultimately aims at providing views on all kinds of issues of interest that are representative for companies in the EU³. This goal can be achieved if there is a sufficient amount of companies participating in the survey that covers the EU Member States, industrial sectors and company size classes such that it is in line with the population distribution of companies in the EU. This in turn requires at least the participation of 2865 companies if a stratified data collection approach is taken in which a certain number of companies is targeted in a country-sector-company size cell⁴. However, as the first consultation made with the EBTP, the European Tax Survey could only cover the 2141 EU companies that were registered at the time in the European Business Test Panel. Furthermore, not all registered companies in the EBTP responded to the questionnaire. At the closure date of the survey 700 EU companies had responded, that is, 32.7% of the registered EU companies participated in the survey. This figure is relatively high compared to participation rates in other international surveys of administrative burdens (see Box 1-2).

³ There is also a targeted number of 127 companies from Norway and Iceland. In total 23 companies from these two countries participated in the European Tax Survey. Given that many questions in the European Tax Survey with respect to cross-border situations were designed for EU countries these two countries are not included in the analysis presented here.

⁴ The collection of data by country-sector-company size cell is cost-effective because it requires less responding companies compared to random selection of companies by country. The targeted number of companies depends on which rule is followed in order to define whether the distribution of companies is in line with the population number of companies (see Annex C for details).

Box 1-2 Response rates in international surveys

The response rate in the European Tax Survey is in line with what could be expected a priori. For tax compliance costs surveys the "normal" response rate is around 30% (See Sandford, 1995, p. 379).

An OECD study on administrative and regulatory burdens has an average response rate of 40% across the participating countries. The response rates in individual countries vary from 18% to 78% (See OECD, 2001).

The response rate in a world wide survey on business obstacles conducted by the World Bank equals 18% for the group of developed countries (See World Bank, 1997).

However, compared to the targeted amount of companies, the number of companies that responded is relatively low. This means that the data of the responding companies does not allow presenting a representative view for the EU companies unless very strong – and unrealistic – assumptions are made about tax issues in the countries and sectors for which no data could be obtained from the survey. Nevertheless, this does not hinder providing an analysis of results linked to the sample itself. After all, 700 EU companies based in 14 Member States provided a unique set of valuable information on the impact of taxation on their decisions and their compliance costs.

In the study, some data and results obtained from the sample responses are presented, without weighting the responses according to their importance in the EU. This data obtained from the companies in the sample gives an insight in the opinions of companies that participated in the sample as such and it provides new evidence on tax obstacles and other issues of taxation. However, this evidence is not representative for the EU Member States that participated in the survey and relates to the companies that responded only. This can be best illustrated by Table C-1 in Annex C, which shows the division of companies that responded over countries and company size. It appears that 37% of the companies that responded are from Denmark and The Netherlands. The over-representation of these countries in the sample implies that an analysis which is based on solely the sample results would put a heavy weight on the opinions of companies in these two countries.

Given the distribution of the responding companies over countries and the topic under consideration in this report, it seems reasonable to weight the opinions of the responding companies in accordance to their presence in the population of companies in the Member States. Therefore, to avoid under and over-representation of certain countries, the opinions of the companies in the sample are weighted in accordance to their actual presence in the EU Member States. This provides evidence of tax obstacles in the EU Member States that participated in the survey which does not overstate the opinions of companies in some countries at the cost of opinions of companies in other Member States.

Before the survey was launched, it was intended to do the weighting by company size, country *and* sector but the number of responses was too low for that. Instead, the number of companies of the same size and of the same country in the populations was used to weight the response of an individual company (see also Box 1-3). Behind this adjustment lies the assumption that assigning equal weight to companies of equal size which are in the same country provides results that reflect better the opinions of

companies in the relevant EU Member States on tax obstacles compared to the other options that would sacrifice either the country aspect or the company size aspect in favor of the industrial sector. Clearly, this choice could lead to distortion in the figures for those topics which are sector specific in some countries or for companies of a certain size. Annex D presents the weighting process in more detail.

Ultimately, the option retained in this study was to present, where possible, both weighted and sample results, while highlighting the merits and limits of both approaches. Whereas both types of results lead to substantially similar results, the authors of this study have focused most of their comments on the weighted results, thereby expressing a preference for results that correct for the under- or over-representation of some countries in the responses obtained from the EBTP. In any event, firm conclusions are only drawn on topics for which the difference between weighted and un-weighted results does not have different qualitative implications regarding tax obstacles in the Internal market. However, it should be kept in mind that none of these results can be considered as fully representative of the EU or the Member States that participated in the survey from a statistical point of view.

Box 1-3 Weighted and sample results

The analysis of Chapters 2 and 3 presents both weighted and un-weighted results.

The un-weighted results give each respondent the same weight and present the opinions of the group of companies that participated in the European Tax Survey. The un-weighted percentages, however, do not reflect the opinions of companies in line with the distribution of companies in the EU Member States that participated in the survey.

In contrast, the weighted results take into account the number of companies "represented" by each respondent⁵. A company is represented by a respondent if it belongs to the same country and to the same company size group as the respondent.

The weighting process is explained in more detail in Annex D.

In the analysis of Chapters 2 and 3 mainly weighted but also un-weighted results are presented. It is made explicit throughout the whole study which results are presented.

1.3.2. Subjective responses

The data collected reflects the opinion of companies for the period in which the survey was conducted. Therefore, in contrast to data collected for official administrative purposes the information is subjective. As such the responses could be influenced by circumstances that prevailed at the time of completion of the questionnaire.

Nevertheless, as a substantial part of the survey contained qualitative questions, this limitation was unavoidable. This may in some cases lead to what may be considered as exaggerated opinions. Nevertheless, the analysis of subjective opinions generally

⁵ The use of sample weights is preferred to the use of economic weights because economic weights are likely to be correlated with compliance costs which is the subject of investigation of Chapter 2.

focuses on differences of results obtained between a set of questions. These underline where the main tax issues lay and what priorities for action could be envisaged.

1.3.3. Bias in the selection of companies

The selection of companies used for the European Business Test Panel was made at the national level by national coordinators in the Member States' administrations. In some countries companies were selected from company data bases at the National Statistic Office. Some other countries selected companies from panels used for other surveys (for example, panels maintained by employer federations) and others outsourced the selection of companies to private sector consulting companies. It can therefore not be completely excluded that in some situations random selection of companies did not take place.

However, it should be noted that registration for the EBTP started well before the launch of the European Tax Survey and most of the companies taking part in the EBTP were not aware of the launch of a tax survey. In addition, clear instructions were sent to national coordinators in charge of inviting company participation to the EBTP (see Annex B). Therefore, it is assumed throughout the study that registration to the panel and participation in the survey occurred in a random way.

1.3.4. Country representation

As a consequence of the limited number of responses to the survey, not all countries are equally represented. For some of the questions relevant to a subgroup of respondents, e.g. firms having a branch, a subsidiary or a permanent establishment in another EU Member State, a more limited number of countries is represented than for those questions asked to all companies in the sample. Therefore, depending on the topic under consideration or the group of companies examined, e.g. SMEs vs. large firms, different groups of countries are represented.

Reporting on only those questions which were answered by the largest set of countries would neglect valuable information on some important topics. Therefore practically all the responses to all the questions are analyzed in this report. Tables included in the Annex C indicate for the different topics which countries are represented.

1.4. Structure of the study

The rest of this study is organised in two main chapters. Chapter 2 presents results on the analysis of compliance costs, while Chapter 3 presents results on tax obstacles to cross-border activities in the European Union.

1.4.1. Compliance costs

Chapter 2 presents the analysis of quantitative data on compliance costs. Although compliance costs are often considered a major problem for companies operating in the Internal market, there are actually few quantitative studies demonstrating this. Whereas several studies on compliance costs can be found in the US, Canada or Australia, there are only a handful of studies for individual EU Member States. Moreover, there has never been a detailed quantitative analysis of compliance costs for several EU Member States.

After briefly presenting the compliance costs data, the results of the regression analysis are presented. This highlights whether and to what extent a number of company characteristics affect compliance costs.

1.4.2. Tax obstacles

Chapter 3 deals with tax obstacles and presents the analysis of the qualitative data obtained from the companies participating to the European Tax Survey. In contrast to the section on compliance costs, which is based on quantitative estimates of compliance costs provided by respondents, this chapter focuses on opinions. Qualitative surveys such as the one presented here have already been undertaken in the past, notably in the context of the Ruding survey (see Box 2-5 below). However, the European Tax Survey is characterized by a particularly large geographical coverage, which also includes countries that acceded to the EU after 1991. Furthermore, the fact that the study includes a quantitative analysis of compliance costs permits a better insight and more detailed results.

The analysis of tax obstacles proceeds in three steps. The opinions of companies on company taxation are examined first. Opinions on VAT are analysed next. Last, the impact of taxation on other issues, such as company structure and investments, as well as financing, is presented. Overall, this section provides an idea of possible impacts of taxation on activities, in particular cross-border activities, of companies in the EU. Explicit links between quantitative results and qualitative results are drawn. It should be noted that whereas the quantitative analysis undertaken in the second chapter indicates which company characteristics are strongly associated with compliance costs, the qualitative analysis aims at providing a more precise insight into the specific influential factors.

The annexes present useful methodological material, detailed results and other useful information to the reader.

2. COMPLIANCE COSTS

2.1. Introduction

The purpose of this chapter is to assess the importance of compliance costs for companies and, in particular, to determine whether cross-border activities imply larger compliance costs. The analysis of annual worldwide compliance costs is based on the estimates provided by the respondents to the European Tax Survey (see Box 2-1), as well as on estimates of the proportion of their worldwide compliance costs relating to five types of compliance costs:

- (1) domestic VAT compliance
- (2) domestic Company Taxation
- (3) other EU Member States' VAT compliance
- (4) other EU Member States' Company Taxation
- (5) any non EU tax related compliance costs

The compliance costs in this study are thus perceived compliance costs as estimated by the respondents and not actual compliance costs that would be measured precisely (see Box 2-2 below). In addition, the compliance costs are gross because possible off-setting benefits of compliance are not taken into account.

Box 2-1 Compliance costs in the European Tax Survey

The question on compliance costs asked to participants was:

"Please estimate [in euros] the annual total worldwide compliance costs incurred when complying with the provisions of company taxation and VAT provisions"

In order to obtain relatively solid information, an indication of the compliance costs to take into account was provided to the respondents:

"Compliance costs include: all the costs related to complying with tax rules and obligations both within and outside the company (e.g. external consultants), in particular, the costs of acquiring information on tax laws and practices, tax obligations (registering, declaration, invoicing, payments and refunds), tax accounting, including tax lawyers, consulting firms, tax audit and litigation. Compliance costs can include salaries (including social security and fringe benefits) or non-personnel costs (e.g. computers). The costs can be incurred within or outside your tax department.

Compliance costs do not include: costs for maintaining or developing a financial accounting system, a management accounting and reporting system or an information system."

The last part was included in order to avoid that more general costs linked to the financial operations of a company would be considered as compliance costs.

It should be noted that the compliance costs examined in the European Tax Survey refer to compliance costs incurred by companies only. Other operating costs of the tax system, such as the administrative costs for the public administration are not analyzed here. Furthermore, other costs of taxation, which may result from tax-induced changes in the structure of prices, are also outside of the scope of this chapter. However, this last issue is dealt with in section 3 of chapter 3.

This chapter presents first some global information on compliance cost after which the results of a more detailed regression analysis are presented. Section 2.2 presents estimates of the absolute total compliance costs and ratios of compliance costs to taxes paid or sales. Results are compared with findings presented in the Ruding report (1991). Section 2.3 introduces the regression analysis. Section 2.4 presents the results of the regression analysis on total compliance costs. Section 2.5 presents the regression results with respect to EU company taxation compliance costs. The results with respect to EU VAT compliance costs are presented in section 2.6. A summary of the main results is provided in section 2.7. Section 2.8 presents the main conclusion of the compliance cost analysis.

2.2. Absolute total compliance costs and the relative burden

This section presents the estimated absolute total compliance costs and their relative burden⁶. Two measures are used for the relative burden of total compliance costs. The first measure is the cost-to-tax-revenue ratio which is the ratio of total compliance costs and taxes. This ratio measures the costs of tax collection in terms of the taxes that are paid by companies. The cost-to-tax-revenue ratio provides a broad indication for governments on the amount of euros companies are required to spend on tax compliance in order to generate a given amount of company tax revenues.

The second measure is the ratio of absolute total compliance costs and sales. This provides an alternative indication of the relative burden of compliance costs. The cost-sales ratio provides a comparison of compliance costs with respect to the output of companies.

Table 2-1 presents the weighted and un-weighted estimates of total compliance costs and its relative burden. The weighted estimates provide a better indication of the situation in the EU countries under investigation while the un-weighted estimates reflect only the situation for the respondents that are included in the sample. This is why in the remainder of this chapter the discussion focuses on the weighted estimates. Annex D shows in detail how the responses are weighted.

The first two lines of Table 2-1 present the estimates of the absolute total compliance costs. The table shows that annual total compliance costs are estimated at €202.000 for SME's compared to €1.470.000 for large companies⁷. The estimated total compliance costs are larger for large companies. It should be noted that the magnitude of the

⁶ See Annex E for the response results on compliance costs.

⁷ Companies with less than 250 employees are referred to as SMEs; companies with 250 or more employees are large companies.

estimated compliance costs for large companies is in line with that obtained in other studies, such as Blumenthal and Slemrod (1995) for large US companies⁸.

Table 2-1 Estimates total compliance costs

	SMEs	Large
Absolute total compliance costs		
(in 1000 euros)		
Weighted average	203	1460
Un-weighted average	984	1662
Absolute total compliance costs/taxes		
(Cost-to-tax revenue ratio)		
Weighted average	30.9%	1.9%
Un-weighted average	15.3%	1.4%
Absolute total compliance costs/sales		
Weighted average	2.6%	0.02%
Un-weighted average	1.3%	0.01%

Note: Percentages in bold are different from zero at a 5% level of significance (see Annex D).

The third line in Table 2-1 presents the weighted estimates for the cost-to-tax-revenue ratio. The amount of taxes paid is information that is provided by the respondents. The results indicate that the relative burden is much lower for large companies compared to SMEs, with a cost-to-tax-revenue ratio of 1.9% and 30.9%, respectively⁹. However, the estimated ratios should be treated with caution because their estimated variances are relatively large, which means there is some uncertainty with these ratios¹⁰.

Box 2-2 Estimated compliance costs versus actual compliance costs

Estimated compliance costs are compliance costs that are estimated by companies. In contrast, actual compliance costs are costs actually paid by the company. Examples of actual compliance costs are the labour costs of staff working in a tax-department and fees paid to tax-consultants.

⁸ Blumenthal and Slemrod (1995) present an average annual compliance costs for large US companies equal to 1.565.100 USD.

⁹ The ratios are calculated as the estimated total worldwide compliance costs divided by the estimated paid taxes. This approach is recommended if the number of respondents is low. See, for example, Scheaffer, Mendenhall and Ott (1990). For SMEs the un-weighted estimate of compliance costs is much higher than the weighted estimate, while for the cost-revenue ratio the weighted estimate is higher than the un-weighted estimate. This happens if those companies reporting high amounts of taxes represent more companies in the population (and receive a higher weight) relative to those companies with high compliance costs.

¹⁰ The hypothesis that the ratios equal zero cannot be rejected at a 5 % level of significance (see annex D for details on this test)

The quality of the results on compliance costs in the European Tax Survey depends on whether the provided estimated compliance costs are biased. On the one hand it could be argued that respondents over-estimate their absolute total compliance costs (Tait, 1988). Those that have high total compliance costs are more eager to participate. A counterargument is that companies with large compliance costs are less likely to participate in surveys as companies that have to meet already many compliance requirements would be less inclined to participate in surveys. Allers (1994) provides evidence for under-estimates of compliance costs.

Although there are no signs that either of the two biases is present in this study one may assume that the estimates in this study could be biased upwards because the compliance costs are estimated compliance costs as opposed to actual compliance costs. Chittenden, Kauser and Poutziouris (2003) present empirical evidence for small companies of over-estimated compliance costs when data on perceived compliance costs is used. These authors compare two studies on VAT compliance costs for small businesses in the UK. One study is based on the perceptions of business owners whereas the other study (Sandford, 1989) measures the actual compliance costs. It turns out that the study measuring actual compliance costs indicates much lower VAT compliance costs expressed in terms of turnover than the study using businesses' perceptions on compliance costs (for some turnover classes actual compliance costs are found to be less than a fifth of those estimated by companies). Chittenden et al. (2003) note: "In fact the SBRT [Small Business Research Trust] data shows that business owners believe that the costs of compliance with government regulations are higher than they are when measured in a structured way". See also Pope (2001) for a short discussion on the differences between actual and compliance costs as estimated by companies.

A comparison with results obtained in international studies is given in Box 2-3 which presents international evidence on cost-to-tax-revenue ratios. This box presents a comparison of cost-to-tax-revenue ratios between different countries and studies. Because of differences in tax systems, data collection and the period for which the ratios are calculated, such a comparison should be considered, at best, as indicative.

The cost-to-tax-revenue ratio estimated in the European Tax Survey for large companies (e.g. 1.9%) is broadly in line with ratios calculated in other studies. There are few comparable cost-to-tax-revenue ratios available for SMEs. A recent finding by Slemrod and Venkatesh (2002) suggests a cost-to-tax-revenue ratio equal to 28.0-29.6% for large and mid-size US companies grouped together¹¹. They argue that for a large part the parents of such companies pay the taxes on the income they generate. That would imply that the estimated cost-to-tax-revenue ratios are upward biased. Slemrod and Venkatesh find lower cost-to-tax-revenue ratios when they take this into account¹².

¹¹ The discussion of the estimated cost-to-revenue ratios in Slemrod and Venkatesh (2002) suggests that their figures are more comparable to the figures for SMEs in this study than the figures for large companies.

¹² Slemrod and Venkatesh (2002) note that a large proportion of large and mid-size companies act as pass-through companies that do not pay tax as their parents pay tax on the income they generate. Taking into account this issue they arrive at a lower estimate equal to 18.3%-19.4%.

The issue of parent companies paying taxes on income generated by SMEs could be equally well present in this study. The estimated 30.9% could therefore be considered as an upper limit of the cost-to-tax-revenue ratio for SMEs.

Note, however, that comparison of cost-to-tax-revenue ratios between different countries and studies is incomplete. As mentioned above, because of differences in tax systems, data collection and the period for which the ratios are calculated, such a comparison should be considered, at best, as indicative.

Box 2-3 International evidence on cost-revenue ratios

USA:	2.9 %	state compliance costs over state taxes for large companies
	1.4 %	federal compliance costs over federal taxes for large companies (Gupta and Mills, 2002)
	28.0%	internal (personnel and non-personnel) and external (outside tax service) compliance costs for large and midsize companies (Slemrod and Venkatesh, 2002)
	29.6%	
		Costs of collecting and remitting sales state and local sales tax over total state and local sales tax revenues in Washington State: 6.5% for small retailers, 3.4% for medium retailers, and 1.0% for large retailers (Washington State Department of Revenue (1998)).
Canada:	3 %	compliance costs over federal and provincial taxes for large companies
	5 %	for <i>Financial Post</i> 500 companies (Erard, 2000)
Australia:		Income tax compliance costs
	6.8 %	for small and large companies together (Tran-nam et al., 2000)
	22.9 %	for small and large companies together (Pope, 1993)
United Kingdom:	2.2 %	(Sandford et al., 1989)
	1.3 %	labour tax compliance costs over tax receipts for small and large companies together (Collard, Green, Godwin and Maskell, 1998)
The Netherlands:	4 %	for small and large companies together (Allers, 1994)
Sweden:	1.3 %	Income tax, payroll taxes, VAT and excise duties for small and large companies together (Malmer in Sandford et. Al., 1995)

The last part of Table 2-1 presents the relative burden of compliance costs measured as compliance costs over sales. The estimated cost-sales ratio for SMEs equals 2.6% compared to 0.02% for large companies. As for the cost-to-tax-revenue ratio, these estimates show that the relative compliance burden is smaller for large companies. Box 2-4 presents the estimated cost-sales ratios for some selected countries.

Box 2-4 International evidence on cost-sales ratios

Canada:	0.10% for companies with turnover between 0.5 million-1 million CAD; 0.06% for companies with turnover above 1 million CAD; Goods and Services Tax Compliance Costs (gross) (Wurts, 1995)
Australia:	0.03% for companies with turnover between 10-50 million NZD; 0.09% for companies with turnover above 50 million (NZD); Income Tax Compliance Costs (Pope, 1993)
New Zealand:	0.03% for companies with turnover between 10-50 million (NZD); 0.09% for companies with turnover above 50 million NZD (Compliance costs with PAYE, Fringe benefits, Goods and Services Tax and Business income tax) (Hasseldine, 1995)
United Kingdom:	0.05% for VAT compliance costs and 0.04% for corporation compliance costs for companies with turnover above 1 million GBP (Godwin, 1995)
The Netherlands:	0.02% for companies with turnover between 100-500 million NLG; 0.006% for companies with turnover above 500 million NLG; compliance costs of tax benefit programmes (Allers, 1994)

The results on the relative burden of compliance costs are similar to results presented in reports by UNICE (1995) and OECD (2001). Both reports indicate a disproportionate burden of compliance requirements for smaller compared to larger companies.

Table 2-2 below presents the composition of EU compliance costs related to company taxation and VAT. These compliance costs are the sum of company taxation and VAT compliance costs in the Home State and in other EU Member States. The percentages in the table are calculated using 80 responses of companies with subsidiaries, branches or permanent establishments abroad that reported compliance costs in all four categories.

It shows the shares of compliance costs attributed to VAT and company taxation at home and abroad. A company with at least one subsidiary abroad is estimated to spend 30% of its EU company taxation and VAT compliance costs on VAT compared to 70% on company taxation. Of the 30% share of VAT compliance costs 19% relates to the Home State while 11% relates to VAT compliance in another EU Member State. The 70% share of company taxation compliance costs relates to 44% in the Home State compared to 26% in another EU Member State.

Table 2-2 Composition EU company taxation and VAT compliance costs (companies with subsidiaries abroad)

VAT compliance costs in:				Company Taxation compliance costs in:			Total
	Home State	Other EU Member States	Both Home State and other EU Member States	Home State	Other EU Member States	Both Home State and other EU Member States	
Weighted	19%	11%	30%	44%	26%	70%	100%
Un-weighted	25%	16%	41%	41%	18%	59%	100%

The figures in Table 2-2 show that the proportion of VAT compliance costs that is made in other EU Member states is 37% (=11/30). For company taxation this proportion is also 37% (=26/70). At first sight this is a surprising finding. A priori one could have expected that the share of foreign compliance costs would be lower for VAT compliance given the large degree of harmonization of VAT legislation already achieved within the EU. For a company that sells products and services abroad, VAT compliance costs abroad consist mainly of filling in and sending the returns. However, there are also VAT procedures which are complicated for companies. An example is the refunding procedure of VAT on inputs incurred in other EU countries. Evidence on this is presented in Section 3-3 of the following chapter.

The information obtained on sales and compliance costs allow for a comparison with two questions included in a survey which are discussed in the Ruding report (see Box 2-5 below). Table 2-3 shows the comparison between the current survey results and those from the Ruding survey¹³. The first two rows indicate the proportion of companies that have a cost-income ratio that falls in the given range. For instance, in the Ruding survey 57.7% of the companies reported a cost-income ratio lower than 1% (see Devereux (1992)).

Similar ratios with respect to sales are presented for the European Tax Survey. The ratios for the European Tax Survey concern revenues from sales only, whereas the Ruding report could also include other income. 78.3% of the respondents to the European Tax Survey reported domestic compliance costs which are less than 1% of revenues from domestic sales, while 78.9% of the respondents reported that foreign compliance costs are less than 1% of revenues from foreign sales.

Both the 1991 and the 2003 results indicate that the percentage of companies with compliance costs less than 1% of income is similar for the domestic and foreign case. The percentage of companies with a cost-income ratio higher than 10% in the European Tax Survey is larger than for 1991, both for the domestic and the foreign case. A

¹³ The questions asked in the Ruding Survey are:

1. "With reference to domestic income, approximately what are the corresponding costs of tax planning and compliance with the provisions of the domestic tax system? Express such costs as a percentage of total domestic source income."

2. "Again with reference to foreign source income, approximately what are the costs incurred by your firm (e.g. tax accounting salaries, fees etc.) in tax planning and complying with the provisions of the domestic tax system? Express such costs as a percentage of the actual income flows net of foreign tax from the foreign source)."

possible explanation is that the 2003 figures are constructed from two questions, one on compliance costs and one on sales. Respondents in the 2003 European Tax Survey did not need to think of the relative burden of compliance costs when participating in the survey. In contrast, respondents in the 1991 survey did have to think on the relative burden of compliance costs as opposed to the absolute magnitude of compliance costs.

Table 2-3 Comparison of compliance cost burden between European Tax Survey (2003) and Ruding survey (1991)

"Ruding survey" 1991	Compliance costs as a fraction of income:					Responses
	Less than 1%	1-3%	3-5%	5-10%	Over 10%	
Domestic Income	57.7%	27.5%	9.7%	4.2%	1.0%	714
Foreign Income	57.4%	29.7%	7.6%	3.4%	2.0%	802

European Tax Survey 2003	Compliance costs as a fraction of revenues from sales:					Responses
	Less than 1%	1-3%	3-5%	5-10%	Over 10%	
Revenues from Domestic sales	78.3%	11.0%	2.8%	2.6%	5.3%	471
Revenues from Foreign sales	78.9%	7.9%	1.7%	3.7%	7.9%	242

The results in Table 2-3 do not necessarily imply that the relative burden of compliance abroad is as costly as at home. For example, it could well be that the mix of companies in the 'domestic' group and the 'foreign' group in the table is the same in terms of activities abroad, position in the corporate group, industrial sector etc. Then, it would be expected to obtain similar percentages.

Box 2-5 The Ruding Report (1991)

As early as 1990, Commissioner Scrivener asked the Committee of Independent Experts on Company Taxation to evaluate the importance of taxation for business decisions. The objective was to determine whether and how taxation could affect the location of investment and the international allocation of profits between enterprises, in order to determine whether existing differences in corporate taxation and the burden of business taxation among Member States led to major distortions affecting the functioning of the Single market. This led to the publication, in 1992, of the *Report of the Committee of Independent Experts on Company Taxation* (also called Ruding Report).

The main findings of the Ruding Report were that tax differences can affect the location of investment and cause distortions of competition (the average cost of capital in every Member State was lowest for purely domestic investments), and that some convergence had happened in the past but the main distortions could not be reduced solely through market forces or through independent action of Member States. The committee issued recommendations that fell essentially into two categories: one on the elimination of double taxation and one on the corporation tax (rate, base, system).

To investigate whether companies that are active abroad face (relatively) high compliance costs compared to domestic companies a regression analysis is more appropriate. The results of the regression analysis are the focus in the remainder of this chapter.

2.3. Regression analysis

The evidence of the previous section shows higher absolute compliance costs and a lower relative compliance burden for large companies compared to smaller companies. To explore further what other company characteristics affect absolute and relative compliance costs the descriptive analysis of the previous section is complemented with a regression analysis. A regression analysis allows focussing on the relationship between compliance costs and several company characteristics rather than one as in the previous section. It has the advantage of considering the impact of one company characteristic, say company size, whilst taking into account other company characteristics that influence compliance costs. In fact, at this stage it is not sure that compliance costs increase because of company size, even though it is likely to be the case. If, for example, the SMEs happen to be just the only companies without activities abroad while all the large companies do operate across the border this could be the explanation for the difference in compliance costs highlighted in the previous section rather than size of the company itself. The use of regression analysis will show whether company size still matters for compliance costs if we take the number of subsidiaries abroad and other company characteristics into account.

This study is not the first that uses regression analysis to identify company characteristics that are correlated with compliance costs. Box 2-6 summarizes common findings by other studies that made use of regression analysis.

Box 2-6 Compliance cost studies using regression techniques

Examples of studies into compliance costs that have made use of regression techniques are Blumenthal and Slemrod (1995) and Mills and Gupta (2002) for the USA, Erard (1997, 2000) for Canada and Verwaal and Cnossen (2000) on intra-EU community VAT compliance costs of companies in The Netherlands.

While these studies make use of different data, model specifications and company characteristics, some common results appear:

- Compliance costs appear to increase with the size of the firm measured by employees, sales or assets.
- Compliance costs increase with the degree of activities abroad.

- Compliance costs appear to increase with the number of members in the corporate group.
- Compliance costs appear to increase with the number of tax regions (provinces or states within a country) in which a company is active.

The presentation of the regression results is divided into three parts. The first part (Section 2.4) presents estimates for the total compliance costs. This will be the leading part in that most of the results for total compliance costs are also found for company taxation and VAT compliance costs. The second part (Section 2.5) presents the results for company taxation compliance costs while the third part (Section 2.6) presents the results with respect to VAT compliance costs. These parts focus on the specific issues relevant for company taxation and VAT compliance costs. Annex F provides detail on the regression analysis and the models that are estimated. In addition, it contains additional tables with results.

Box 2-7 Model specification issues

The presented results have been obtained after some data checks and model specification tests. First it should be mentioned that not all available company characteristics are included because of collinearity, that is correlation, between the company characteristics. A limited set of company characteristics is included based on its relevance for compliance costs and some evident cases of collinearity. A particular example of collinearity is related to the size of a company for which both the number of employees and sales could be used. Sales and the number of employees in the company are strongly correlated (see also Box 3-4 for correlation between these two characteristics) and are not included together in the model that is used to estimate the relationship between compliance costs and company characteristics. The number of employees is used as an indicator of the size of a company whereas sales is used to construct a variable to measure the burden of tax compliance for companies.

The results presented in the following sections follow a test that was conducted to investigate non-linearities in the relationship between compliance costs and company characteristics. For all presented results a non-linear specification of the model was rejected against a linear specification.

Additionally a test to discriminate between un-weighted estimation of the model and weighted estimation of the model indicated that the un-weighted estimates of the model are rejected in favour of the weighted estimates¹⁴. Therefore, the weighted results are preferred and presented in this chapter and the un-weighted results are presented in Annex F.

¹⁴ To discriminate between the un-weighted and the weighted results, the test introduced by Dumouchel and Duncan (1983) and further discussed by Winship and Radbill (1994) is used. The preferred estimates of the model to describe the relationship between compliance costs and its determinants are the weighted ordinary least squares (WOLS) estimates using the non-zero responses on worldwide compliance costs (see Annex F for details on the regression analysis and the un-weighted regression results).

A final issue to discuss before presenting the results is the issue of measurement error in the data and its consequences for the analysis. Box 2-2 indicates that the compliance costs reported by the respondents may be higher than the actual compliance costs made by companies. The potential measurement error in compliance costs implies that the dependent variable in the regression models is subject to measurement error. However, measurement error in the dependent variable forms a part of the error term in the model describing compliance costs. If the assumptions made on the error term in the model are valid, the measurement error in compliance costs does not affect the estimated correlations with company characteristics. A problem could arise if a certain specific group of companies is more likely to overestimate its actual compliance costs. In that case, the estimated correlations between compliance costs and the company characteristics that characterize that group are likely to be upward biased. While there is evidence on the perception of high compliance costs by respondents (see Box 2-2) there is no empirical evidence available yet on whether certain groups of companies are more likely to perceive higher compliance costs compared to other groups. Therefore, the regression analysis is based on the assumption that this type of measurement error is likely to affect the reported compliance costs by each company in the analysis to the same extent.

In contrast to measurement error in compliance costs, the presence of measurement error in the company characteristics used to explain compliance costs would bias the estimated coefficients of those company characteristics in the model. However, the company characteristics used in the models are straightforward to measure and did not require deep inquiries or guesswork by the respondents.

2.4. Total compliance costs

Table 2-4 below presents the set of company characteristics used for the total compliance costs regressions. It can be noted that all variables included in the models are so-called "dummy-variables". For the characteristic company size, micro companies are the reference. Similarly, the other company characteristics also have a reference category. Overall, the reference company in the regression is an Austrian micro company without a subsidiary, branch or permanent establishment and active in the Mining/Quarrying sector. The reference categories are not included in the Table 2-4.

Table 2-4 Company characteristics included in the model

Small	dummy variable equal to one if company size is small; equal to zero otherwise A company is small if it has 10 or more but less than 50 employees.
Medium	dummy variable equal to one if company size is medium; equal to zero otherwise A company is medium if it has 50 or more but less than 250 employees.

Large	dummy variable equal to one if company size is large; equal to zero otherwise A company is large if it has more than 250 employees.
Parent with subsidiaries in Home State	dummy variable equal to one if company has a subsidiary, branch or permanent establishment in the Home State; equal to zero otherwise
Parent with subsidiaries, branch or permanent establishment in other EU Member States	dummy variable equal to one if company has a subsidiary, branch or permanent establishment elsewhere in the EU; equal to zero otherwise
Control variables	sector dummies, country dummies and a dummy variable indicating whether the accounting year ended in 2003

The control variables indicated in the table are included in order to estimate the effects of company characteristics on total compliance costs *net* of country and sector effects on compliance costs. The variable indicating whether the accounting year ended in 2003 captures possible changes in tax systems that were introduced early 2003 or possible (short term) differences in the economic situation.

Box 2-8 presents the expected relationship between total compliance costs and company characteristics.

Box 2-8 Expected results for total compliance costs

Company Size

It can be expected that total compliance costs are higher for large companies. In contrast, a lower relative burden of total compliance costs for large companies is expected.

Parent companies with subsidiaries in the Home State

It can be expected that parent companies with subsidiaries, branches or permanent establishments (hereafter "companies with subsidiaries"). in the Home State are faced with higher compliance costs compared to companies without subsidiaries. For the relative burden of compliance costs it is not a priori clear whether parent companies with subsidiaries in the Home State have lower or higher compliance costs relative to sales than companies without subsidiaries, branches or permanent establishments.

Parent companies with subsidiaries in other EU Member States

Parent companies with subsidiaries abroad are expected to have higher compliance costs than companies without subsidiaries. The compliance costs relative to sales of parent companies with subsidiaries, branches or permanent establishments abroad could be lower or higher compared to companies without subsidiaries.

Number of Subsidiaries/branches/permanent establishments abroad

Given the complexities of operating in other Member States with different languages and tax systems it can be expected that companies with subsidiaries abroad have higher total compliance costs than companies without subsidiaries abroad. As concerns the intensity of the presence abroad it can be expected that more subsidiaries abroad results in more compliance costs. For the relative burden of total compliance costs it seems reasonable to expect the same regressive effect for the number of subsidiaries abroad as for company size. If a regressive effect is present, the relative total compliance burden for companies with subsidiaries abroad would decrease with the number of subsidiaries.

Cross-border compliance cost effect

It is important to note that the inclusion of a variable for parent companies with subsidiaries in the Home State and a variable for parent companies with subsidiaries in other EU Member States allows investigation of a cross-border effect. The estimated coefficients of these variables provide insight in differences between compliance costs of parent companies with subsidiaries in the Home State and parent companies with subsidiaries in other EU Member States given the other company characteristics that are included in the model.

Table 2-5 shows the estimated relationship between total compliance costs and the company characteristics in Table 2-4. Models 1 and 2 present the results for the absolute total compliance costs. Model 2 differs from the first model in that it considers the *number* of subsidiaries, branches or permanent establishments abroad rather than only the incidence of subsidiaries, branches or permanent establishments abroad.

In addition, results are presented with respect to the relative total compliance costs. The relative burden is measured by the fraction of sales that a company spends on total compliance costs. Measuring the relative burden in terms of sales as opposed to taxes is preferred because sales reflect better the size of the company and the economic output of a company¹⁵. The difference between Model 3 and 4 is that Model 3 includes the incidence while Model 4 includes the number of subsidiaries, branches or permanent establishments abroad. The number of observations included in the sample for Models 1 and 2 and Models 3 and 4 are different because some companies did not report sales. For these companies compliance costs cannot be expressed in terms of sales¹⁶.

¹⁵ In addition, using sales instead of taxes to measure the relative compliance costs implies that more companies can be included in the regression analysis.

¹⁶ This applies also for the reported regression results with respect to company taxation and VAT compliance costs in the following sections.

Table 2-5 Total compliance costs

	Model 1	Model 2	Model 3	Model 4
Dependent variable	Compliance costs (1000 euros)	Compliance costs (1000 euros)	Compliance costs/sales	Compliance costs/sales
Company Characteristics				
Small	0.585 (0.553)	0.581 (0.552)	-0.194 (0.539)	-0.197 (0.540)
Medium	1.349** (0.606)	1.324** (0.609)	-1.645** (0.650)	-1.670** (0.648)
Large	2.176*** (0.754)	1.974*** (0.702)	-2.695*** (0.698)	-2.201*** (0.656)
Parent with subsidiary/branches/ permanent establishments in Home State	0.306 (0.297)	0.290 (0.298)	-0.250 (0.372)	-0.273 (0.376)
Parent with subsidiary/branches/ permanent establishments in other Member States	1.679*** (0.583)	-	0.715 (0.601)	-
Sub/branch/PE in other Member States: 1-5	-	1.891** (0.777)	-	1.260** (0.535)
Sub/branch/PE in other Member States: 6-15	-	2.130*** (0.412)	-	0.328 (0.621)
Sub/branch/PE in other Member States: 16-50	-	3.490*** (0.948)	-	-3.053** (1.316)
Sub/branch/PE in other Member States: >50	-	0.588 (0.657)	-	-0.629 (0.835)
2003	-0.002 (0.304)	0.011 (0.305)	0.545 (0.460)	0.563 (0.465)
<i>Sectors (10)</i>	Yes	Yes	Yes***	Yes***
<i>Countries (12)</i>	Yes**	Yes**	Yes	Yes
Adjusted R ²	0.267	0.267	0.240	0.250
Observations	572	572	534	534

- Notes:
- i) Estimation method: Weighted OLS with constant included.
 - ii) ***, **, *, denote, respectively, significance at 1, 5, 10% level.
 - iii) Standard deviations of the coefficients are in parentheses and robust against any form of heteroskedasticity.
 - iv) Compliance costs and its relative burden are in logarithms. Zero observations on compliance costs have been excluded.

Box 2-9 Interpreting the results - Graphs

For the interpretation of the coefficients, the reference company is an Austrian micro company without a subsidiary, branch or permanent establishment and active in the Mining/Quarrying sector. This means that, for example, the coefficient on "small" indicates the total compliance costs relative to micro companies given all other included company characteristics.

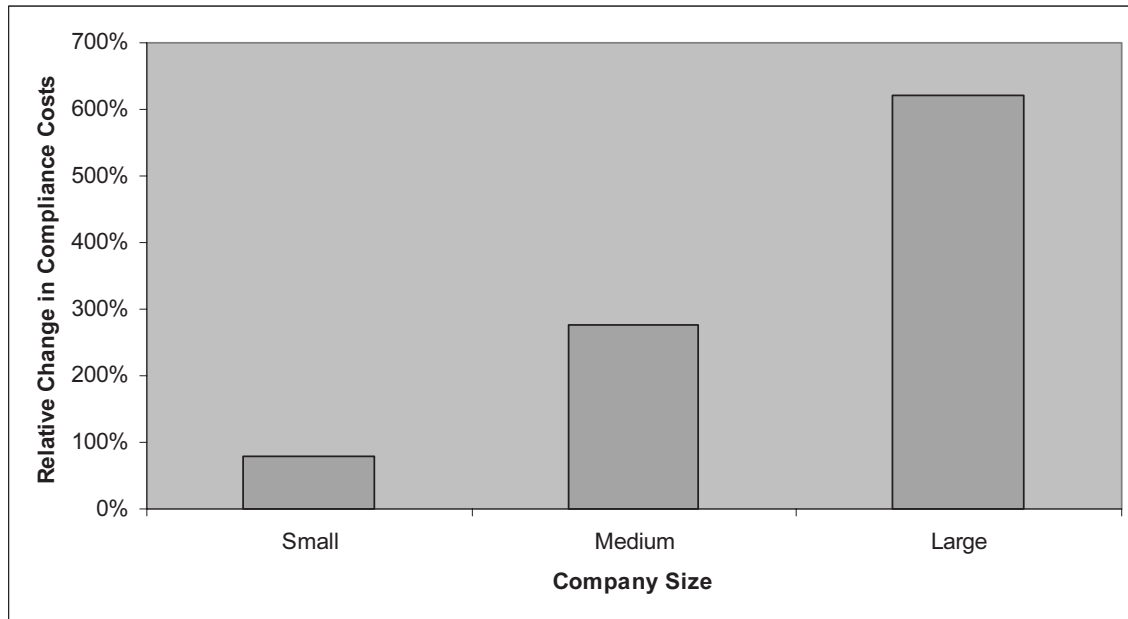
The model is estimated in logarithms such that the coefficients do not indicate differences in euros. For example, the correct interpretation of the estimated coefficient equal to 0.581 for small companies in the second column of Table 2-5 is that given the included company characteristics in the model, small companies appear to have total compliance costs which are 1.88 times higher than for micro companies. This figure is calculated as the ratio of the exponential of 0.581 (which is 1.88) divided by the exponential of zero (which is equal to one and refers to the reference group which is micro companies for this example). Hence, in percentages compliance costs for small companies are, *ceteris paribus*, 188% times higher than for micro companies. This is equivalent to 88 percentage-points more compliance costs than for micro companies. This corresponds to the height of the bar for small companies in Graph 2-1 below. The advantage of using changes in %-points compared to the change in percentages is that it is more clear whether compliance costs are higher or lower than the comparison company.

It should be stressed, however, that the relative comparisons can be high in some cases as the graphs are constructed given the other company characteristics in the model. That is, the regression model used to construct the graphs only explains part and not all of the compliance costs. Some company characteristics are important but could not be included in the model, e.g. number of different States in which a company operates. Therefore, the graphs serve to indicate the relative importance of company characteristics with respect to compliance costs.

2.4.1. Company size

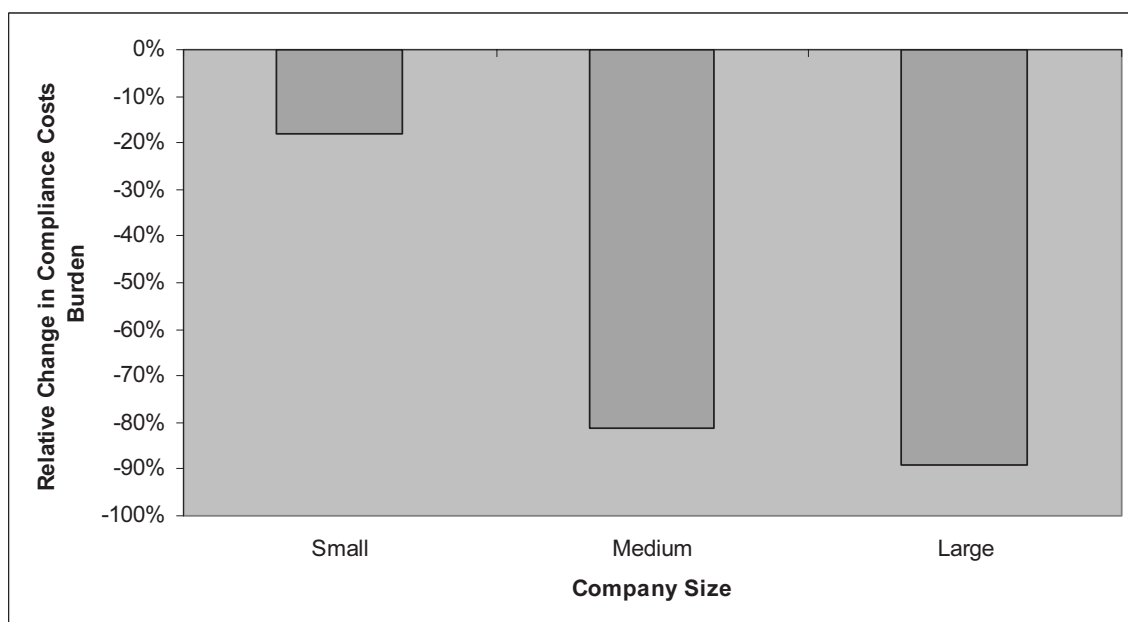
The results with respect to total compliance costs in the second column of Table 2-5 show that total compliance costs are increasing with company size. Based on the estimated coefficients in the table, Graph 2-1 presents the estimated percentage increase in compliance costs for small, medium and large companies compared to micro companies.

Graph 2-1 Total compliance costs (small, medium and large companies compared to micro companies)



Graph 2-2 shows the relative compliance costs as a percentage of sales for small, medium and large companies compared to that of micro companies (based on the estimates of Model 4 in Table 2-5). It follows that total compliance costs expressed in terms of sales decrease with company size. This result is a well established result in the literature on compliance costs and could reflect that a part of the tax compliance costs for EU companies is a fixed cost or that there are economies of scale in meeting compliance requirements.

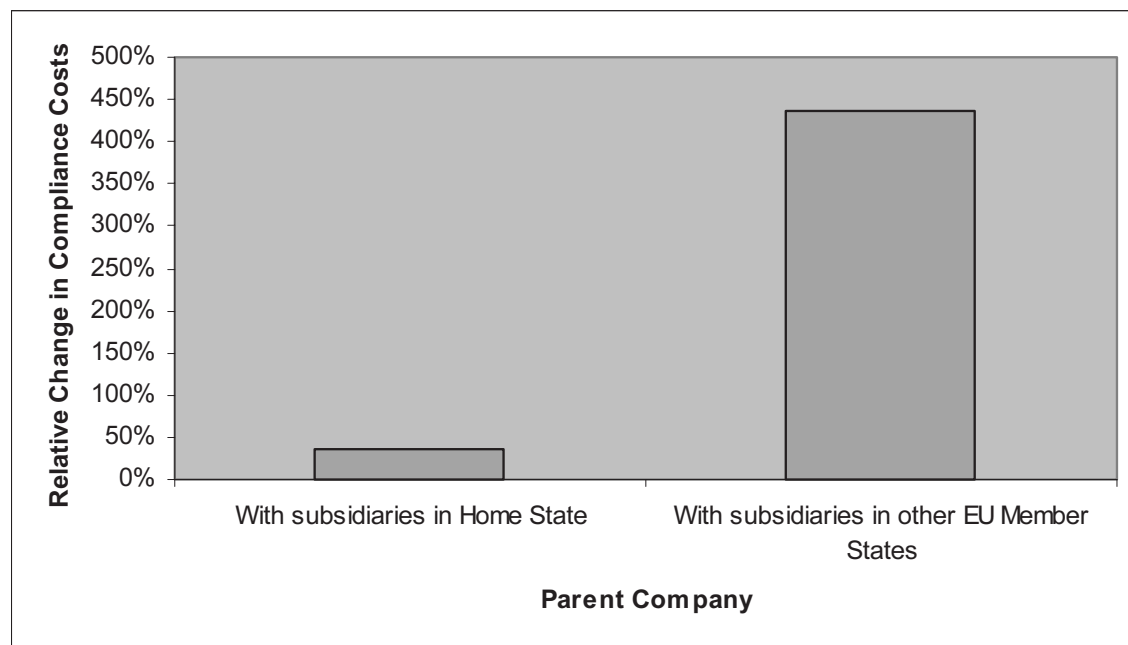
Graph 2-2 Total relative compliance costs as a fraction of sales for small, medium and large companies compared to micro companies



2.4.2. Cross-border effect in compliance costs

The estimates indicate that parent companies have higher compliance costs than non-parent companies (see Model 1 in Table 2-5), *ceteris paribus*. However, a parent company with subsidiaries in the Home State does not appear to have compliance costs that are significantly different from those of a company without subsidiaries. In contrast, a parent company with subsidiaries, branches or permanent establishments in other EU Member States appears to have significantly higher compliance costs than companies without subsidiaries. In addition, the hypothesis that a parent company with subsidiaries, branches or permanent establishments in the Home State has the same amount of compliance costs as a parent company with subsidiaries, branches or permanent establishments in other EU Member States is rejected¹⁷. This suggests that a cross-border effect is present and that parent companies with subsidiaries abroad appear to have more compliance costs compared to parent companies with subsidiaries, branches or permanent establishments in the Home State and companies without any subsidiaries, branches or permanent establishments. Graph 2-3 illustrates the differences in compliance costs of parent companies compared to companies without subsidiaries, branches or permanent establishments.

Graph 2-3 Total compliance costs of parent companies compared to companies without subsidiaries, branches or permanent establishments



With respect to the burden of compliance costs the estimates show (see Model 3 Table 2-5) a negative effect for parent companies with subsidiaries in the Home State and a positive coefficients for parent companies with subsidiaries, branches or permanent

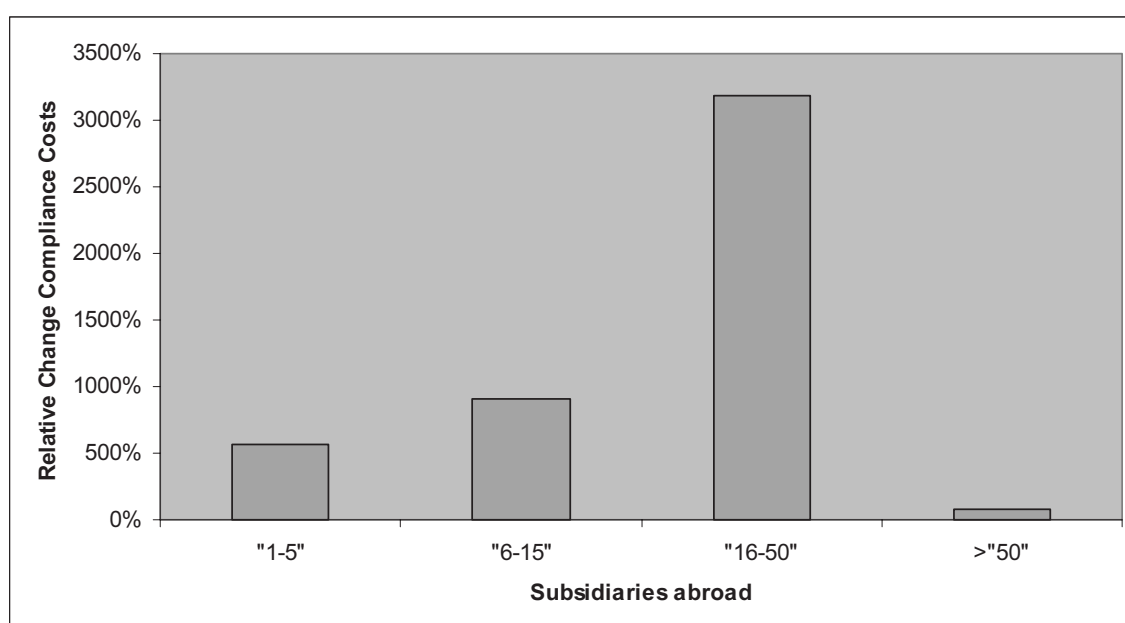
¹⁷ The performed F-test rejects equality of the coefficients of the two type of parent companies (p-value equals 0.034).

establishments in other EU Member States. The estimates are not significantly different from zero, however.

2.4.3. *Subsidiaries, branches or permanent establishments abroad*

Model 1 in Table 2-5 shows that parent companies with a subsidiary, branch or permanent establishment abroad appear to have more compliance costs compared to parent companies with a subsidiary, branch or permanent establishment in the Home State and companies without a subsidiary, branch or permanent establishment. Model 2 in Table 2-5 investigates whether the number of subsidiaries abroad matters. It follows that more subsidiaries abroad are associated with more total compliance costs. This becomes clear in Graph 2-4 which is based on the estimated coefficients of Model 2¹⁸.

Graph 2-4 Total compliance costs of company with subsidiaries, branches or permanent establishments abroad compared to domestic companies¹⁹



The results with respect to the compliance costs relative to sales show a slightly different picture (see Model 3 in Table 2-5). The estimated coefficient for parent companies with a subsidiary, branch or permanent establishment abroad is positive but not significantly different from zero.

Concerning the relationship between relative compliance costs expressed in terms of sales and the number of subsidiaries abroad the weighted estimates of Model 4 in Table

¹⁸ The estimated coefficient for the variable “More than 50 subsidiaries, branches or permanent establishments abroad” is very small and indicates that the total compliance costs are not different from domestic companies. It is unlikely that this result reflects reality and has economic significance.

¹⁹ The estimated coefficient for companies with more than 50 subsidiaries, branches or permanent establishments abroad is very small and not significantly different from zero.

2.5 suggest a decreasing pattern in compliance costs relative to sales and the number of subsidiaries abroad. For companies between six and fifteen subsidiaries abroad the compliance costs relative to sales are not statistically different from companies without a subsidiary abroad (see fourth column Table 2-5). Companies with between sixteen and fifty subsidiaries abroad appear to have a lower relative compliance burden compared to companies without a subsidiary abroad. Companies with more than fifty subsidiaries again show lower compliance costs in terms of sales compared to companies without a subsidiary abroad but the estimated coefficient is not significantly different from zero. However, it should be noted that the estimated pattern between the number of subsidiaries abroad and compliance costs is not present in the corresponding un-weighted results for which none of the estimated coefficients of the "subsidiaries abroad" variables is statistically significant (see Table F-3 in Annex F). This raises the possibility that the estimated pattern arises for computational reasons and does not reflect economic significance. Further checks on the data confirm this possibility²⁰ and imply that the sample size is too small to draw firm conclusions with respect to the relation between the number of subsidiaries abroad and total compliance costs relative to sales.

2.4.4. *Sector differences*

The tests on the joint significance of the included sector variables suggests that their inclusion in the model helps in explaining the relative burden of the compliance costs (see third and fourth column of Table 2-5). The information on sectors and countries is included in the regression analysis to control for possible unobserved sector and country effects²¹. However, the estimated coefficients on sectors could be subject to response-bias. Also, the results are weighted by the population of companies in each company-size-country cell. The weighting procedure did not take into account differences among sectors (see Chapter 1). This could have implications for the estimated coefficients of the sector variables. Hence, both un-weighted and weighted results are likely to be subject to some bias.

Given these caveats both the weighted and un-weighted results suggest that, *ceteris paribus*, total compliance costs are lowest in the following four sectors: Hotels, Restaurants and Bars, Real Estate, Health and Social Work and other Community Services²². Concerning the total compliance cost relative to sales, a comparison between the weighted and the un-weighted results suggests that the burden of total compliance costs is highest in the sector Hotels, Restaurants and Bars. Both weighted and un-weighted results indicate that the total compliance costs relative to sales are low in the sectors Wholesale and retail trade and Financial Intermediation.

²⁰ In the sample, some micro, small and medium companies reported to have more than 15 subsidiaries abroad. Re-estimation of model 4 with these companies excluded from the sample resulted in a significant estimated coefficient, equal to 1.258 for the variable "1-5 subsidiaries abroad". No significant estimates are obtained for the coefficients of the three other variables indicating the number of subsidiaries abroad.

²¹ Or unobserved variables that affect compliance costs of companies which are captured by the inclusion of the sector and country variables.

²² The estimated coefficients on all company characteristics (including sector and country) can be found in Annex F.

2.5. Company taxation compliance costs in the EU

In the previous section the focus was on total worldwide compliance costs. This section analyses the determinants of EU company taxation compliance costs only. The data used was calculated on the basis of the share of EU company taxation compliance costs related to total worldwide compliance costs provided by respondents.

In addition to the set of company characteristics used to investigate the total worldwide compliance costs (see Table 2-4), variables such as information on mergers and acquisitions and transfer pricing, could be a relevant factor for company taxation compliance costs. The questionnaire used for the European Tax Survey contained some qualitative information on these issues that could also be used for the econometric analysis. Table 2-6 shows the two extra company characteristics included in the regressions for company taxation compliance costs.

Table 2-6 Additional company characteristics used for the analysis of company taxation compliance costs

Merger	dummy variable equal to one if a company has merged with or acquired another company during the last five years; equal to zero otherwise
Transfer Pricing	dummy variable equal to one if a company has been subject to an examination by a tax administration on its intra-group cross-border transactions during the last five years; equal to zero otherwise.

The expected relation between company taxation compliance costs and merger and transfer pricing is outlined in Box 2-10. For the expected results with respect to the other included company characteristics see Box 2-7.

Box 2-10 Expected results company taxation compliance costs

Transfer Pricing

A positive relationship between reported company taxation compliance costs and the transfer pricing variable is expected. Reasons for this are the extra time or staff that is needed for justification of the documents after an investigation by the tax authority. The fact that transfer pricing relates to cross-border operations of companies could magnify such effects. It is expected to see the positive relationship for both total compliance costs and compliance costs as a percentage of sales.

Mergers & Acquisitions

As concerns the relationship between total compliance costs and the merger and acquisitions variable both a negative and a positive relationship could be expected. A negative relationship can be expected if the merger has been fully accomplished and synergies materialized in less compliance requirements. On the other hand if the merger took place recently the merged company could face additional compliance requirements and a positive relationship can be expected. It is difficult to anticipate possible differences for merged companies between total compliance costs and compliance costs relative to sales.

Table 2-7 shows the results of the analysis for company taxation compliance costs. The results of the first model show similar findings as for total compliance costs: company taxation compliance costs increase with company size and company taxation compliance costs relative to sales decrease with company size.

Table 2-7 Company taxation compliance costs

	Model 1	Model 2	Model 3	Model 4
Dependent variable	Compliance costs (1000 euros)	Compliance costs (1000 euros)	Compliance costs/sales	Compliance costs/sales
Company Characteristics				
Small	0.030 (0.595)	0.051 (0.591)	-0.333 (0.658)	-0.343 (0.649)
Medium	0.786 (0.716)	0.767 (0.730)	-1.752** (0.859)	-1.819** (0.879)
Large	1.406** (0.601)	1.292** (0.591)	-2.222*** (0.798)	-1.961** (0.793)
Transfer Pricing	1.022** (0.496)	0.856* (0.476)	0.091 (0.762)	-0.098 (0.667)
Merger	0.616* (0.365)	0.575 (0.375)	0.888* (0.488)	0.918* (0.498)
Parent with subsidiary/branches/permanent establishments in Home State	-0.017 (0.484)	-0.033 (0.488)	-0.557 (0.621)	-0.568 (0.622)
Parent with subsidiary/branches/permanent establishments in other Member States	1.530*** (0.478)	-	-1.078** (0.560)	-
Sub/branch/PE in other Member States: 1-5	-	1.814*** (0.678)	-	-0.636 (0.757)
Sub/branch/PE in other	-	1.626***	-	0.275

Member States: 6-15		(0.537)		(0.700)
Sub/branch/PE in other Member States: 16-50	-	2.723*** (1.083)	-	-3.832* (1.548)
Sub/branch/PE in other Member States: >50	-	1.220 (0.834)	-	-1.390 (0.850)
2003	-0.097 (0.369)	-0.114 (0.376)	0.390 (0.545)	0.364 (0.545)
<i>Sectors (10)</i>	Yes***	Yes***	Yes***	Yes***
<i>Countries (11)</i>	Yes***	Yes***	Yes	Yes
Adjusted R ²	0.403	0.400	0.242	0.243
Observations	477	477	444	444

- Notes:
- i) Estimation method: Weighted OLS with constant included.
 - ii) ***, **, *, denote, respectively, significance at 1, 5, 10% level.
 - iii) Standard deviations of the coefficients are in parentheses and robust against any form of heteroskedasticity.
 - iv) Compliance costs and its relative burden are in logarithms. Zero observations on compliance costs have been excluded.

Models 1 and 2 show that company taxation compliance costs for parent companies with foreign subsidiaries, branches or permanent establishments in other EU Member States are higher compared to parent companies with subsidiaries, branches or permanent establishments in the Home State and companies without subsidiaries, branches or permanent establishments²³. The estimates further show that company taxation compliance costs increase with the number of foreign subsidiaries, branches or permanent establishments abroad. The estimation results of models 3 and 4 in Table 2-7 show that parent companies with foreign subsidiaries, branches or permanent establishments in other EU Member States have lower company taxation compliance costs expressed in terms of sales compared to parent companies with subsidiaries, branches or permanent establishments in the Home State and companies without subsidiaries, branches or permanent establishments. The estimated negative coefficient of parent companies with subsidiaries, branches or permanent establishments abroad is significantly different from zero. This is a result that did not appear for total compliance costs and it suggests a, *ceteris paribus*, lower burden of compliance costs for parent companies with subsidiaries, branches or permanent establishments abroad. However, the un-weighted estimation results suggests the opposite effect for parent companies with foreign subsidiaries, branches or permanent establishments in other EU Member States which avoids being conclusive on this effect. The results also show that the company taxation compliance costs tend to decrease in terms of sales if the number of subsidiaries, branches or permanent establishments abroad increases but, as in the case for total compliance costs, the limited sample size does not permit drawing firm conclusions on this pattern.

²³ The performed F-test rejects equality of the coefficients of the two type of parent companies (p-value equals 0.038).

In addition, companies that have been subject to a transfer-pricing investigation have higher compliance costs compared to companies that were not subject to such an investigation. As concerns mergers, companies that merged or acquired another business appear to have company taxation compliance costs that are higher than companies that did not, though the estimated effect is not very precise²⁴.

If the number of subsidiaries, branches or permanent establishments abroad is taken into account, the estimated coefficient of the transfer pricing variable is significant at the 10% level (see Model 2 in Table 2-7) whereas it is strongly significant if only the presence of at least one subsidiary abroad is taken into account (which what the variable "parent company with subsidiaries, branches or permanent establishments in other EU Member States" measures). Companies with several subsidiaries abroad are more likely to get involved in transfer pricing and hence to be subject to investigations on transfer pricing. As the results indicate, like in the case of total compliance costs, companies with more subsidiaries abroad are associated with higher company taxation compliance costs. It appears that in the first model in Table 2-7 the transfer price variable picks up part of the effect of being present abroad with several subsidiaries. Nevertheless, the second model indicates that even if the number of subsidiaries is taken into account, a transfer pricing investigation is positively associated with company taxation compliance costs.

As concerns the sector differences in company taxation costs the weighted and un-weighted results indicate that company taxation compliance costs are lowest in the following four sectors: Real Estate, Health and Social Work and other Community Services. The same caveats apply for these estimates as for the estimated sector differences for total compliance costs. The weighted and un-weighted results further indicate that the company taxation costs and the company taxation compliance costs expressed in terms of sales appear highest in the Mining sector.

2.6. VAT compliance costs in the EU

This section presents the results with respect to VAT compliance costs. These were calculated using the share of total compliance costs that respondents indicated to spend on VAT compliance requirements.

Before turning to the results of the regressions, it is useful to discuss the specification of the models used in this section. With respect to VAT, the difficulty in modelling compliance costs arises from the various situations that can lead to VAT compliance costs. This applies in particular to the cross-border operations of a company in relation to VAT. There are three major situations in which a company faces VAT compliance costs abroad.

- (1) VAT compliance costs that are related to VAT activities abroad with a subsidiary, branch or permanent establishment (e.g. sales through a subsidiary abroad).

²⁴ The estimated coefficient of the merger variable is significantly different from zero at the 10% level only.

- (2) VAT compliance costs that are related to VAT activities abroad without a subsidiary, branch or permanent establishment. An example is an architect that sells its services to a client abroad in the EU.
- (3) VAT compliance costs related to VAT incurred on input. An example is a transport company whose trucks cross an EU foreign country to deliver products in a third country. If trucks stop to buy diesel in the country which is crossed VAT is paid on the diesel. In this case the transport company can, under the 8th directive, obtain a refund of the VAT incurred on input (diesel in this example).

Since the procedures related to VAT compliance are not the same for these different situations, the situations have to be taken into account in the analysis with respect to VAT compliance cost. In relation to this, it is important to note that companies can operate in different countries at the same time. For example, the transport company in country A can have an establishment in country B and at the same time buy diesel in country C. Hence, it would have a VAT registration number in country B while being entitled to obtain refunds under the 8th Directive in country C. The consequence is that companies could face the three different situations in different countries.

To a certain extent the data obtained from the European Tax Survey allows for distinction between the possible combinations of situations that could arise and which are relevant for VAT compliance costs. For each company it is known whether situations 1, 2 and 3 apply to its operations abroad. Companies were asked to indicate whether they have a subsidiary, branch or permanent establishment abroad, whether they undertake VAT activities in another EU Member State in which they do not have a permanent establishment and whether they incurred VAT on inputs abroad in another EU Member State. By combining the responses of a company in relation to these three situations part of the multiple state operations of a company can be captured. However, recall that the European Tax Survey does not provide information on the specific State nor the number of States to which cross-border situations apply. By combining the information provided by respondents on the three cross-border VAT situations a distinction can be made between eight types of companies as listed in Table 2-8.

Table 2-8 Partition of companies by cross-border VAT situation

			Subsidiaries, branches or permanent establishments abroad?	
			No	Yes
VAT incurred on inputs abroad?	No	VAT activities in another EU Member State without having a permanent establishment there?	No	Type 1
			Yes	Type 2
	Yes	VAT activities in another EU Member State without having a permanent establishment there?	No	Type 3
			Yes	Type 4
			Type 5	Type 6
			Type 7	Type 8

The eight types of companies listed in Table 2-8 above capture to a certain extent the degree with which a company operates across borders. For example, a company of type 1 can be called purely domestic as it has no subsidiary, branch or permanent establishment abroad, it does not have VAT activities in another EU Member State and it did not incur VAT on inputs in another EU Member State. In contrast, the company of type 8 has subsidiaries, branches or permanent establishments abroad, undertakes VAT activities in at least one EU Member State where it does not have subsidiaries, branches or permanent establishments and incurs VAT on inputs in another EU Member State. In between type 1 and type 8 companies are companies that have a combination of the three cross-border VAT situations. That is, one or two out of the three cross-border VAT situations apply for companies of types 2-7. Box 2-11 presents the expected results with respect VAT compliance costs and the eight different types of cross-border VAT situations for companies. Companies of type 1 are the reference category in the model and therefore no coefficient is reported for this company characteristic in Table 2-9.

Box 2-11 Expected results for VAT compliance costs

As concerns VAT compliance costs it can be expected that a company of type 8 that is involved in all three cross-border VAT situations at the same time faces the highest compliance costs. In addition, it seems also reasonable to expect that companies with a subsidiary, branch or permanent establishment abroad, i.e. types 5-8, do have more VAT compliance costs compared to domestic companies of type 1-4.

Within the group of domestic companies, types 1-4, and the group of multinational companies, types 5-8, it can be expected that companies with VAT activities in another EU Member State without a physical presence there that incurred VAT on input, i.e. types 3, 4 and 7, 8 respectively, face much higher VAT compliance costs compared to companies that do not have either VAT activity.

The differences between the eight cross-border VAT situations are also expected to apply for compliance costs expressed in terms of sales.

It should be remarked that the expectations with respect to the VAT compliance costs are made under the assumption that the degree of activity in each of the three cross-border VAT situations is similar. This assumption is necessary because information that is not contained by the European Tax Survey is the frequency and size of a company's VAT activities in an EU Member State without a subsidiary, branch or permanent establishment there. Nor does the European Tax Survey contain information on the number of times VAT is incurred on inputs in another EU Member State.

In addition to the different types of cross-border VAT situations the basic set of company characteristics used for the analysis of total compliance costs (see Table 2-4) is included in the models for VAT compliance costs. In contrast to company taxation compliance costs, there are no a priori reasons to expect a relationship between mergers and acquisitions or transfer pricing investigations and VAT compliance costs. Therefore, mergers and acquisitions and transfer pricing are not included in the models for VAT compliance costs.

Table 2-9 shows the results with respect to VAT compliance costs. The same basic results are obtained for VAT compliance costs as for total compliance costs (see Model 1 in Table 2-5). In particular, VAT compliance costs appear to increase with company size and VAT compliance costs relative to sales decrease with company size. The results also show the presence of a cross-border effect for the amount of VAT compliance costs expressed by the estimated coefficients of the parent company variables. The estimates indicate that parent companies with subsidiaries, branches or permanent establishments abroad have higher VAT compliance costs than parent companies with subsidiaries, branches or permanent establishments in the Home State²⁵. In turn, the parent companies with subsidiaries, branches or permanent establishments in the Home State appear to have higher VAT compliance costs than companies without subsidiaries, branches or permanent establishments. For the total compliance costs and company taxation compliance an increasing pattern is found for the amount of compliance costs and the number of subsidiaries abroad.

²⁵ The performed F-test rejects equality of the coefficients of the two type of parent companies (p-value equals 0.086).

Table 2-9 VAT compliance costs

	Model 1	Model 2	Model 3	Model 4
Dependent variable	Compliance costs (1000 euros)	Compliance costs (1000 euros)	Compliance costs/sales	Compliance costs/sales
Company characteristics				
Small	-0.016 (0.425)	0.343 (0.382)	0.551 (0.616)	-0.322 (0.593)
Medium	0.581 (0.524)	0.796* (0.472)	-2.193*** (0.727)	-1.834*** (0.651)
Large	0.972** (0.454)	1.095** (0.452)	-3.472*** (0.747)	-2.976*** (0.693)
Parent with subsidiary/branches/ permanent establishments in Home State	0.710* (0.386)	0.718** (0.299)	0.062 (0.446)	0.182 (0.418)
Parent with subsidiary/branches/ permanent establishments in other Member States	1.768*** (0.398)	-	0.857 (0.902)	-
<u>Domestic Companies without a subsidiary, branch or permanent establishment in other Member States:</u>				
2. Only foreign VAT activities without physical presence	-	-2.519*** (0.415)	-	-0.844 (0.606)
3. Only VAT incurred on inputs abroad	-	-0.773** (0.384)	-	-1.413*** (0.621)
4. Both foreign VAT activities without physical presence and VAT incurred on inputs abroad		0.782** (0.305)		-0.210 (0.535)
<u>Companies with a subsidiary, branch or permanent establishment in other Member States:</u>				
5. No foreign VAT activities without physical presence and no VAT incurred on inputs abroad	-	1.260*** (0.448)	-	0.739 (1.170)
6. Only foreign VAT activities without physical presence	-	0.911 (1.476)	-	0.087 (1.212)
7. Only VAT incurred on inputs abroad	-	3.767*** (0.530)	-	0.743 (0.779)
8. Both foreign VAT activities without physical presence and VAT incurred on inputs abroad		3.374*** (0.970)		-0.845 (0.739)
2003	-0.456 (0.373)	-0.724** (0.334)	-0.351 (0.492)	-0.405** (0.427)
<i>Sectors (10)</i>	Yes***	Yes***	Yes***	Yes***

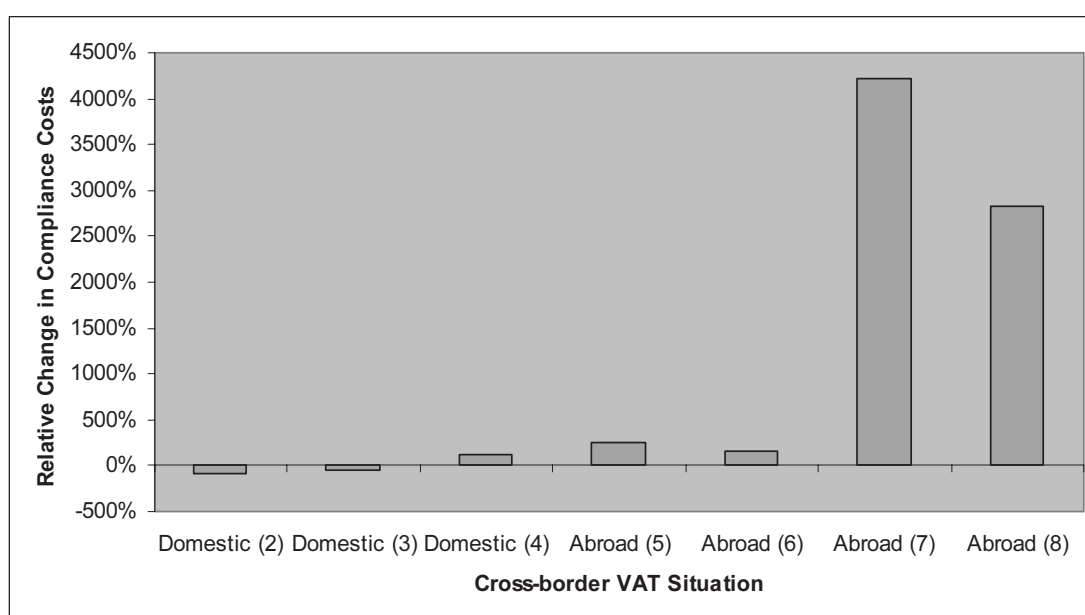
<i>Countries (12)</i>	Yes ***	Yes ***	Yes	Yes
Adjusted R ²	0.423	0.543	0.289	0.326
Observations	487	487	455	455

- Notes:
- i) Estimation method: Weighted OLS with constant included.
 - ii) ***, **, *, denote, respectively, significance at 1, 5, 10% level.
 - iii) Standard deviations of the coefficients are in parentheses and robust against any form of heteroskedasticity.
 - iv) Compliance costs and its relative burden are in logarithms. Zero observations on compliance costs have been excluded.

This result is confirmed for VAT compliance costs by the results of model 2 shown in Table F-11 in Annex F.

Model 2 in Table 2-8 shows the estimation results when distinguishing between the eight types of cross-border VAT situations outlined earlier in this section. The reference type of company is a domestic company that has no VAT activities abroad without a permanent establishment nor does it incur VAT on inputs abroad (type 1 in Table 2-8). Graph 2-5 shows the differences in VAT compliance costs with respect to the different VAT situations.

Graph 2-5 VAT compliance costs for companies with different types of cross-border VAT situations compared to pure domestic company



The results in Graph 2-5 show that type 7 and type 8 companies have the highest VAT compliance costs. These are the companies with a subsidiary, branch or permanent establishment abroad that incurred VAT on inputs (type 7) and, additionally, have VAT activities abroad without an establishment (type 8).

As could be expected all four types of companies with subsidiaries abroad show higher compliance costs compared to purely domestic companies of type 1. No large differences in VAT compliance costs appear to exist between type 5 companies that

only have a subsidiary, branch or permanent establishment abroad and type 6 companies with a subsidiary, branch or permanent establishment abroad that only have VAT activities without an establishment. As concerns domestic companies, those with VAT activities abroad without a permanent establishment (type 2) show lower VAT compliance costs compared to purely domestic companies of type 1. A similar result is obtained for type 3 companies without a subsidiary, branch or permanent establishment abroad that only incur VAT on input abroad. These results are contrary to the expectations. However, it could be attributed to a relatively low degree of VAT activities for these types of companies in the sample. Unfortunately, this issue cannot be explored further as there is no information available on the frequency and size of a company's VAT activities in an EU Member State without a subsidiary, branch or permanent establishment there. Nor does the European Tax Survey contain information on the number of times VAT is incurred on inputs in another EU Member State.

In contrast, domestic companies which have VAT activities in another EU Member State and incur VAT on inputs abroad (type 4) show higher VAT compliance costs compared to type 1 domestic companies.

The results on the VAT compliance costs relative to sales (see Model 4 in Table 2-12) do not show convincing evidence of differences in the relative burden of VAT compliance costs among the different VAT situations²⁶. The only statistically significant estimate is that of domestic companies that incurred VAT on inputs abroad. As for the absolute compliance cost, the sign is negative and in contrast with what would have been expected.

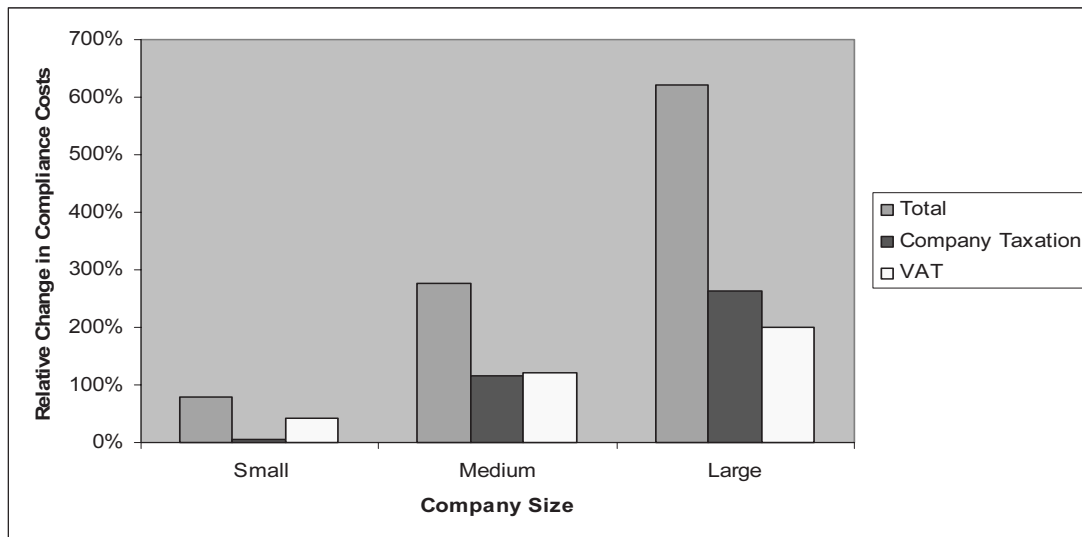
As concerns the sector differences in VAT compliance costs the un-weighted results suggest that VAT compliance costs are relatively low in the real estate and health sectors and VAT compliance costs appear high in the electricity sector. Here the same caveats apply as for the estimated sector differences for total compliance costs. As concerns the VAT compliance costs expressed in terms of sales, the weighted and un-weighted results seem to suggest that the real estate sector experiences the highest burden of VAT compliance costs.

2.7. Overview and comparison

Taking together the results of the regression analysis several common results have been found for company taxation, VAT and total compliance costs. First, compliance costs increase with the size of the company. This applies to company taxation, VAT and total compliance costs as depicted in Graph 2-6.

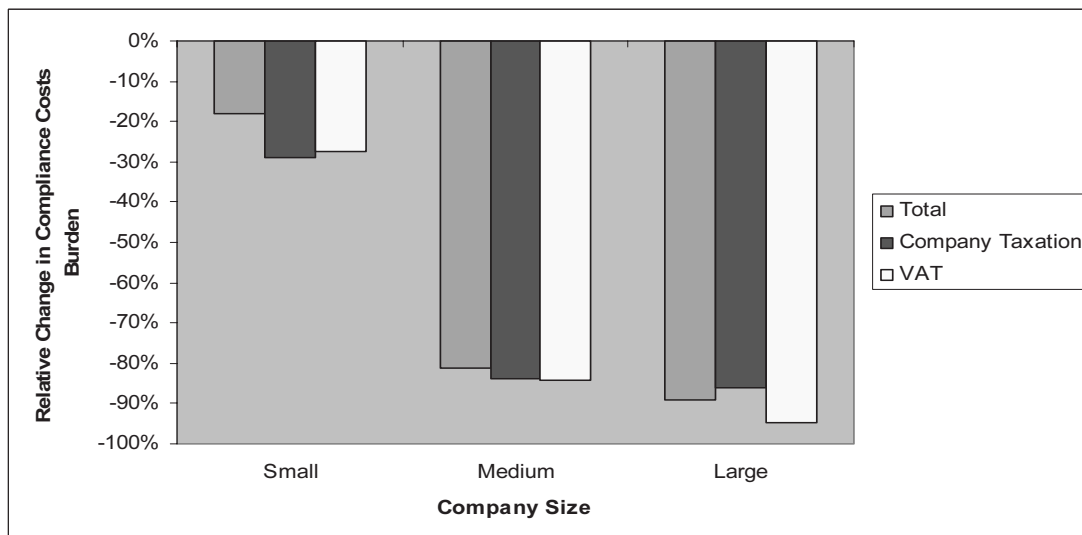
²⁶ No graph is constructed for the VAT compliance costs expressed in terms of sales because most of the estimated coefficients are not significantly different from zero.

Graph 2-6 Compliance costs of small, medium and large companies compared to micro companies

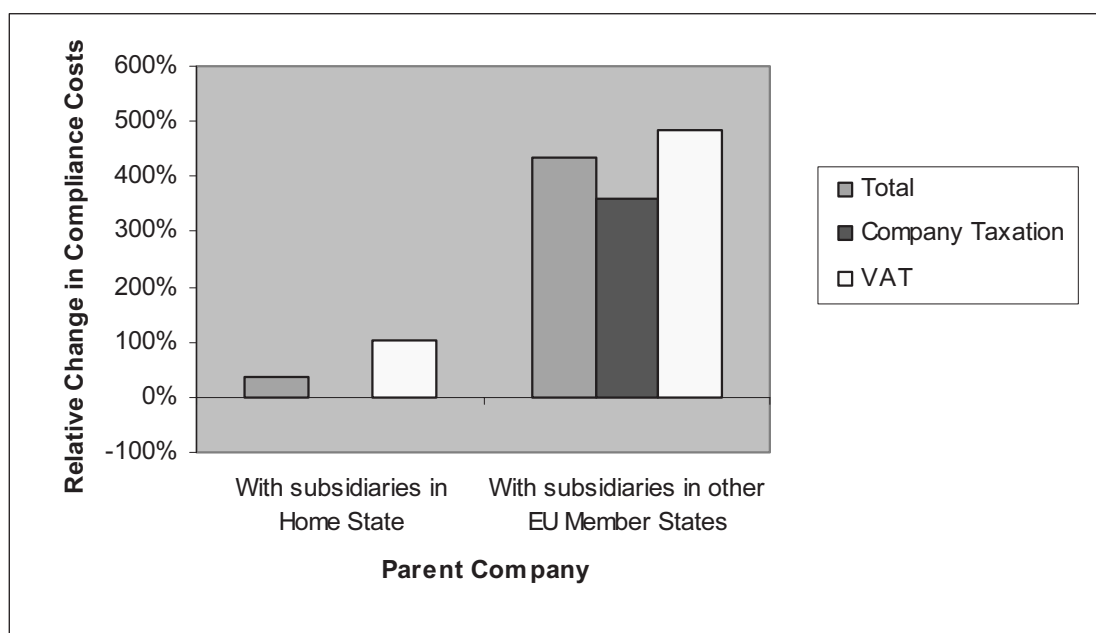


The compliance costs increase with company size. However, compliance costs as a percentage of sales decrease with company size. This is a fairly robust result which is in line with the literature. Graph 2-7 shows the decreasing pattern in the burden of compliance costs for VAT, company taxation and total compliance costs, respectively.

Graph 2-7 Compliance costs relative to sales for small, medium and large companies compared to micro companies



Graph 2-8 Compliance costs of parent companies compared to companies without subsidiaries, branches or permanent establishments²⁷

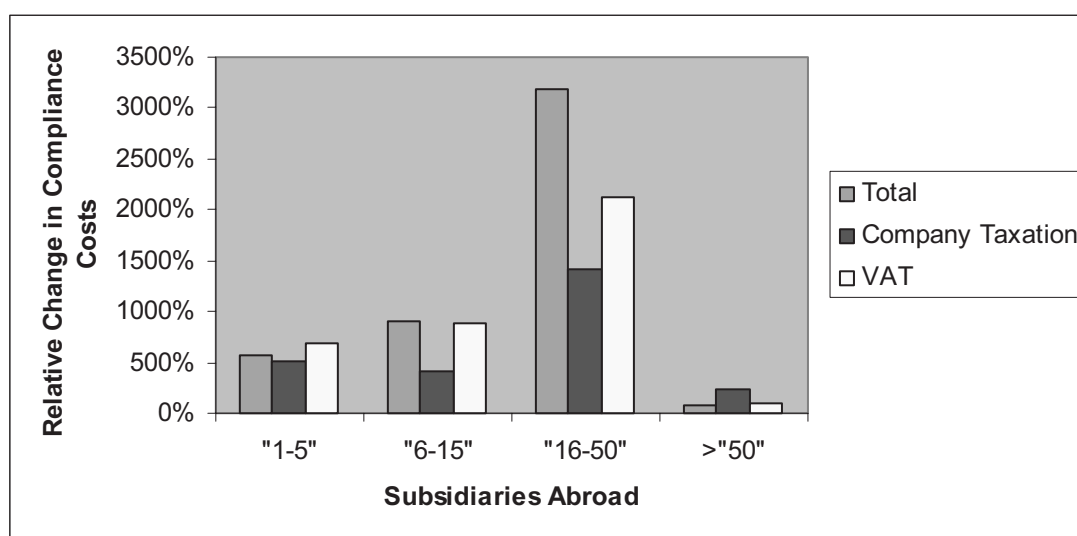


Graph 2-8 shows the cross-border effect of compliance costs and indicates that parent companies with subsidiaries, branches or permanent establishments in other EU Member States face higher compliance costs than parent companies with subsidiaries, branches or permanent establishments in the Home State. Both types of parent companies face higher compliance costs compared to companies without any subsidiaries, branches or permanent establishments, *ceteris paribus*.

The last result illustrated in Graph 2-9 below shows that companies with subsidiaries, branches or permanent establishments abroad have more compliance costs than domestic companies with or without subsidiaries at home. It should be noted that the amount of compliance costs of companies with subsidiaries, branches or permanent establishments abroad depends on their number. The compliance costs increase with the number of subsidiaries up to 50. For companies with more than 50 subsidiaries, branches or permanent establishments no statistically significant compliance costs difference from domestic companies is obtained. The estimated small difference in compliance costs for these companies compared to domestic companies is unlikely to reflect economic significance.

²⁷ For company taxation, the estimated coefficient for parent companies with subsidiaries in the Home State is negative, very small and not significantly different from zero.

Graph 2-9 Compliance costs for companies with subsidiaries, branches or permanent establishments abroad compared to domestic companies²⁸



With respect to the differences in compliance costs across sectors, the results suggest that VAT, Company Taxation and total compliance costs are relatively low in the Real Estate sector and the Health sector. The financial intermediation sector appears as the sector in which the compliance costs expressed in terms of sales are low compared to other sectors.

2.8. Conclusion

The measurement of compliance costs is particularly difficult because compliance costs cover a number of expenses incurred in different parts of a company (and its branches, subsidiaries or permanent establishments) and can involve external services, such as legal advisors. In addition, compliance costs estimated by companies may be higher than the actual compliance costs. Therefore, any measure of compliance costs provided in the context of the European Tax Survey should be considered with these caveats in mind.

The following main result is drawn concerning the extent of companies' compliance costs.

Compliance costs are estimated at €203.000 for SMEs and €1.460.000 for large companies. These amounts correspond to 30.9% and 1.9% of taxes paid and to 2.6% and 0.02% of sales, respectively. The figures for large companies are consistent with figures presented in other studies. Though there are few comparable figures for SMEs, an established finding in the economic literature is that compliance costs ratios tend to decrease with the size of companies. These results should be taken with caution, in particular the results concerning SMEs. Evidence for the US suggests that the high

²⁸ For total compliance costs, the estimated coefficient for companies with more than 50 subsidiaries, branches or permanent establishments abroad is very small and not significantly different from zero.

percentage for compliance costs relative to taxes paid for SMEs could arise because their taxes are paid for them by their parent company.

Gross figures also indicate that the share of foreign compliance costs is similar for VAT and company taxation compliance costs for companies with subsidiaries, branches or permanent establishments abroad that face both types of compliance costs both in the Home State and in other Member States.

In order to complement and refine the analysis of the descriptive results obtained for compliance costs, a regression analysis was undertaken. Four main results should in particular be underlined.

- First, it is shown that the absolute total compliance costs, as well as compliance costs related to company taxation and VAT increase with company size. Furthermore, the relative burden of compliance costs (as a percentage of sales) decreases with company size. This can be explained by the fixed cost nature of tax compliance costs and of regulation costs in general or by possible economies of scale in meeting the tax compliance requirements. The results on compliance costs and company size are consistent with those obtained by other studies.
- Second, compliance costs related to company taxation and VAT and total compliance costs are, *ceteris paribus*, higher for parent companies with at least one subsidiary, branch or permanent establishment in another EU Member State compared with parent companies with subsidiaries, branches or permanent establishments in the Home State. Moreover, the compliance costs increase with the number of subsidiaries abroad, *ceteris paribus*.
- Third, VAT compliance costs appear particularly high for companies that undertake activities in other EU Member States without having a permanent establishment there and companies that incur VAT on inputs in other EU Member States.
- Fourth, a number of more specific findings can also be underlined. The regression analysis shows that companies which have been submitted to transfer pricing controls have higher company taxation compliance costs compared to companies not submitted to such controls.

The regression analysis provides evidence for the hypothesis that the existence of different tax systems in the EU, both for VAT and company taxation, imposes larger costs on companies having cross-border activities. Companies with subsidiaries abroad face higher compliance costs related to company taxation and VAT compared to domestic companies. In particular, companies that are involved in different cross-border VAT situations at the same time appear to have relatively large amounts of VAT compliance costs. Among these types of companies are probably companies that have subsidiaries in some states, undertake VAT activities in other EU Member States where they do not have an establishment and also incur VAT on inputs in other EU Member States.

3. TAX OBSTACLES

3.1. Introduction

The previous chapter on compliance costs demonstrates the company characteristics that are strongly correlated with compliance costs. In particular, from the responses obtained in the European Tax Survey, it can be shown that large companies are associated with more absolute compliance costs but with a lower relative burden (as a percentage of sales or taxes paid). The regressions also suggest that compliance costs of companies increase with the number of subsidiaries abroad, *ceteris paribus*. Most importantly, *ceteris paribus*, a company operating in foreign EU Member States will face higher compliance costs than a similar company operating only on its domestic market.

These results are particularly important because they help us identifying the groups of companies that suffer disproportionately from tax compliance requirements in the European Union. Nevertheless, in a more operational perspective, they do not help much in proposing remedial solutions to that problem. This is why a better insight into companies' specific difficulties related with compliance requirements in the company taxation and VAT areas is particularly useful.

This chapter aims precisely at highlighting the main problems encountered by companies with regard to compliance requirements, both in a domestic context and in cross-border activities. Thanks to the opinions provided by companies in the European Tax Survey, it is also possible to identify what could be possible priorities for action in order to facilitate the operation of companies active in the Internal market.

In what follows, various dimensions of tax obstacles to cross-border activities in the Internal market are examined. The first section focuses specifically on company taxation. Based on responses obtained in the Survey, it aims at identifying the main difficulties encountered by companies regarding the compliance requirements for domestic and foreign-sourced incomes. Questions are as specific as possible in order to delineate areas for possible future action. A number of questions deal with mergers and acquisitions and transfer pricing at the end of the first section. The second section focuses on VAT compliance requirements. The approach follows closely the one of the first section, which facilitates comparisons of results on company and VAT compliance requirements. This is particularly useful since VAT is largely harmonised at EU level, while this is hardly the case for company taxation. One therefore expects some differences in results. Specific questions on the 8th VAT directive and issues encountered by companies having VAT activities in another Member State without having a permanent establishment are dealt with at the end of this section. The third section focuses on the impact of tax systems on important facets of companies' activities in the EU. The link between taxation and investments and the absence of cross-border VAT activities is examined first. The impact of taxation on the company structure and financing is examined next. The conclusions present the main results of the section.

Before turning to the analysis of qualitative responses, it should be noted that many results are presented in the format of graphs. These usually indicate results in simplified form. In particular, where respondents could introduce nuances in their responses, the graphs tend to simplify and give less nuanced information, e.g. "moderately difficult" and "very difficult" are grouped under "difficult". This allows a quicker perception of the main information, at the cost of a more refined presentation. Nevertheless, where necessary this information is completed by a number of more detailed tables. Furthermore, the text provides appropriate comments where more refined results are necessary.

In addition, the issue of country representation discussed in Section 1.3 of Chapter 1 needs to be recalled. Considering the size of the sample, it may be that the country representation corresponding to some groups of companies differ, e.g. for micro vs. medium companies, SMEs vs. large companies, companies with a subsidiary, a branch or a permanent establishment abroad vs. other companies. Therefore, comparisons between such groups implicitly assume that interchanging the group of represented countries with each other does not distort the comparison that is made. This is a strong assumption as there can be differences in opinions on tax obstacles across countries. The issue of country representation is mainly relevant where there are comparisons for a selected subgroup of companies, e.g. comparisons of results for SMEs and large companies with a subsidiary, a branch or a permanent establishment abroad. However, it can be verified in Annex C that when comparisons are made for responses to questions involving all companies of the EBTP there is a large overlap of countries. Furthermore, there are no such problems when different questions among the same group of companies are considered, e.g. opinions of large companies on several issues related to company taxation in the domestic context. Further information on country representation can be found in Annex C.

Besides, it is essential to stress that the results presented below do not pretend to be representative of the EU or the Member States of companies participating in the Survey. Despite attempts to extrapolate the results through a weighting process, the number of responses involved does not permit drawing results that are statistically representatives for the whole of the EU (see Section 1.3.1 above).

3.2. Company taxation

The first part of the qualitative questions deals with company taxation. The respondents provided first information as to a number of potential tax issues in the domestic context. The same questions were then asked with regard to foreign-sourced income. The replies to these questions are provided in turn. These are then compared in order to identify situations in which cross-border activities may be hindered due to tax issues.

In what follows, reference will sometimes be made to two important past studies on company taxation, namely the Ruding report and the Commission study on company taxation in the Internal market [SEC(2001)1681]. These are briefly summarised in Box 2-5 in Chapter 2 and in Box 3-1 below, respectively.

Box 3-1 Company taxation in the internal market

The Ruding report (see Box 2-5) met only with a very limited success and its recommendations were hardly taken up. Ten years later, the Council asked the Commission to carry out a comprehensive study on company taxation. In accordance with the Council's mandate, this study [SEC(2001)1681] illustrated in various scenarios for inbound and outbound investments the existing differences in (marginal and average) effective corporate tax rates of Member States, analysed tax-induced distortions and corporate tax obstacles to cross-border economic activities in the Internal Market and assessed possible remedial measures thereto.

As regards its first part, the study found that taxation is only one of the determinants of investment and financing decisions. Effective tax rates differentials are high inside the EU (up to 30 percentage points). The overall national nominal tax rate is the most relevant component of the effective tax rate while the tax base has only a relatively little impact on the effective tax rate. Given some methodological caveats and that no analysis of the evolution of effective tax rates over time had been carried out and that the effects of tax competition could not be modelled, it was however not possible to assess the size of possible welfare losses associated with the existing differences in effective rates of corporate taxation in the EU Member States. Therefore, the Commission concluded in 2001 that specific actions on the approximation of the national corporate tax rates or the fixing of a minimum corporate tax rate were not necessary at this point in time.

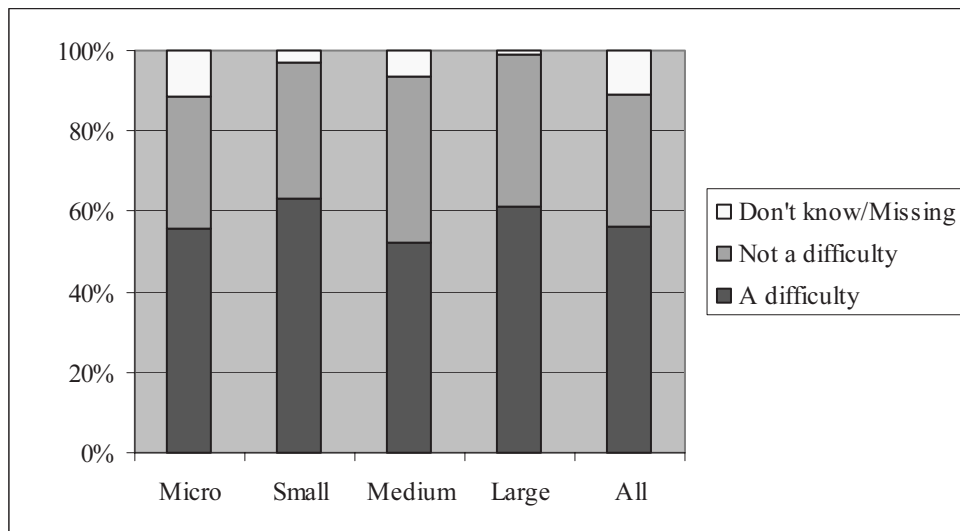
The tax obstacles to cross-border economic activities in the Internal Market which were identified and considered in detail concern, among other things, certain deficiencies of the existing EU tax directives (e.g. their narrow scope), double-taxation treaties, the taxation of cross-border restructuring operations, the lack of cross-border loss-offset, numerous transfer pricing issues and, last but not the least, the compliance cost resulting from the very fact that companies in one Internal Market have to deal with up to 15 (now 25) tax systems. The solutions that were elaborated include both targeted, short-term measures and the comprehensive, longer-term approach of providing companies with a common consolidated tax base for their EU-wide activities. This common tax base could be established on the basis of the national rules of the home state of the parent company of an EU-wide group or, more ambitiously, by compiling a genuinely new EU tax base. The Commission subsequently took most of these up in its Communication "Towards an Internal Market without tax obstacles. A strategy for providing companies with a consolidated corporate tax base for their EU-wide activities" [COM(2001)582].

3.2.1. Company taxation issues related to domestic income

Question:

"Complying with Company Tax legislation and procedures relating to domestic incomes may sometimes present difficulties. Some of these are listed below. Please give your opinion on each of them."

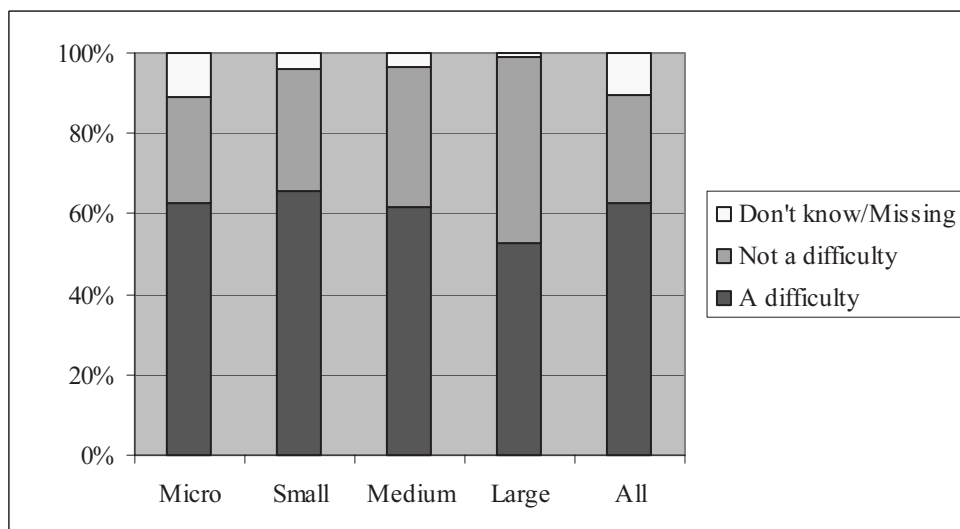
Graph 3-1 Opinions on tax accounting and record keeping (weighted results)



Note: Results based on the 700 responses obtained in the European Tax Survey

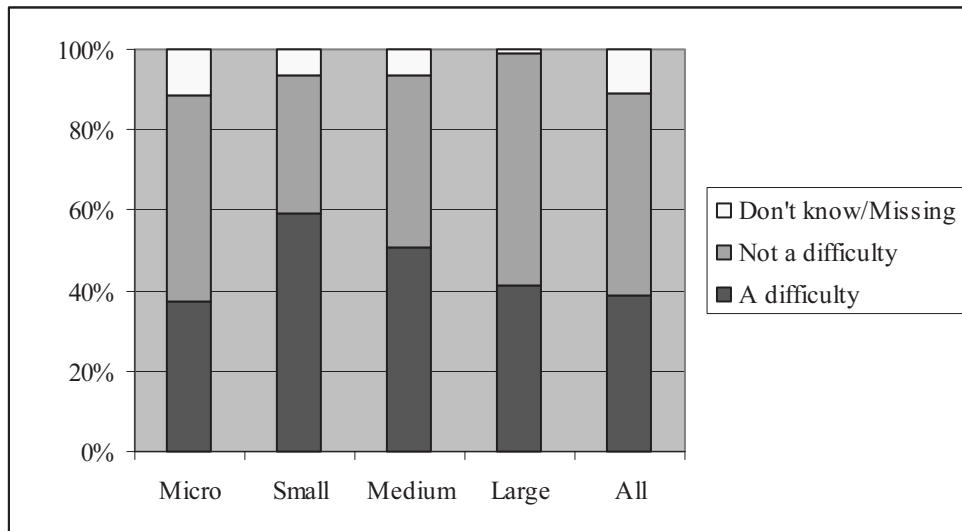
The weighted results based on the 700 responses to the European Tax Survey, illustrated by Graph 3-1, indicate that 56.0% of all companies have at least some difficulties with complying with the tax accounting and record keeping obligations in their home country (see percentages in Table 3-1 below). This is also the case for each category of companies: 55.6% of the micro companies, 63.1% of the small companies, 52.4% of the medium-sized companies and 61.2% of the large companies.

Graph 3-2 Opinions on acquiring information on tax laws and regulations (weighted results)



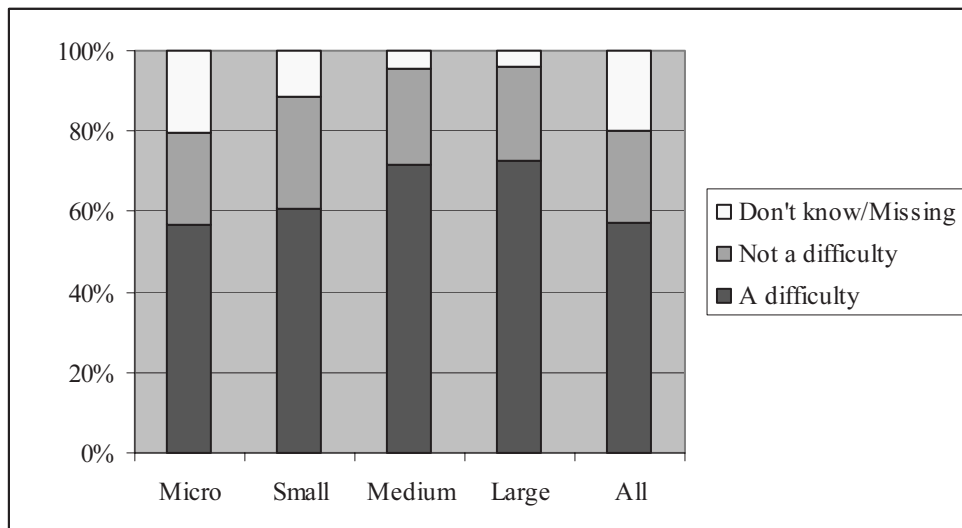
The weighted figures in Graph 3-2 indicate that 62.6% of companies have some difficulties acquiring information on tax laws and regulations in their home country. More than 50% of companies of all sizes have difficulties in this respect. However, with the exception of micro companies the figures suggest that the larger the company the less difficult it is to obtain information.

Graph 3-3 Opinions on contacting tax administrations or tax officials (weighted results)



The weighted estimates presented in Graph 3-3 indicate that 50.4% of companies do not encounter particular difficulties for contacting tax administrations or tax officials. Again, it is worth noting that, with the exception of micro companies, the larger the company the less difficult it seems to be to contact tax administrations.

Graph 3-4 Opinions on audits and litigation (weighted results)

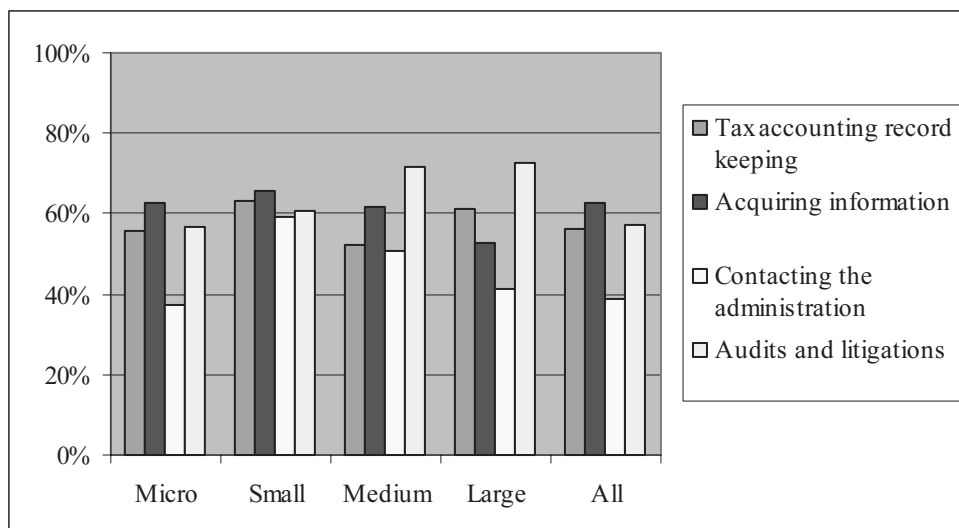


Concerning audits and litigations, the weighted results in Graph 3-4 illustrate that 57.1% of companies have difficulties in the domestic context. Here, difficulties increase with the size of companies. Whereas an estimated 56.8% of micro companies have difficulties, 72.7% of large companies report difficulties. It is also interesting to note that the percentage of responses in the "missing/don't know" category decreases with the size of companies, which suggests that the question is more applicable to larger companies, who are more likely to have experience of audits and litigation given the larger amounts of tax at stake.

Comparison and overview:

The following Graph 3-5 presents an overview of the responses of companies in the domestic context.

Graph 3-5 Comparison of results (% of companies indicating difficulties for various issues – weighted results)



Three main results can be underlined from Graph 3-5. First, the weighted results based on the responses in the EBTP indicate that more than 50% of companies expressed difficulties for all issues related to complying with domestic tax regulations, except contacting tax officials or administrations. Second, the issue that raises most concern for micro and small companies is the one that relates to acquiring information about tax law and regulations. Third, the issue of audits and litigations seems to be a particular concern to medium and large companies. In two instances (acquiring information and contacting administrations), the difficulties expressed by companies diminish with their size, which could reflect some economies of scale or specialisation. However, this does not seem to be the case for micro companies, which report less difficulties on average than small companies. This may be due to these companies relying on their professional advisors to provide information and contact administrations rather than trying to do this for themselves. Alternatively, this may reflect a different country representation as was indicated in the introduction to this chapter. Lastly, it may simply reflect lower requirements being imposed on the smallest companies. More research could usefully be undertaken in that area.

Table 3-1 below shows the weighted percentages from which the graphs above were derived, as well as the un-weighted percentages. In most cases there are no major differences between the weighted and the un-weighted results. This table brings additional information as it presents detailed results concerning the degree of difficulty, i.e. "a moderate difficulty" vs. "an important difficulty", encountered by companies with regard to the issues examined.

Table 3-1 Opinions on tax issues related to domestic income

Company size	Weighted percentages					Unweighted (sample) percentages				
	Micro	Small	Medium	Large	All	Micro	Small	Medium	Large	All
Tax accounting/record keeping is										
Not a difficulty	32.8	34.1	41.1	38.0	33.0	34.9	42.2	42.2	39.2	39.7
A moderate difficulty	42.3	49.2	35.4	48.1	42.6	43.9	42.9	41.0	46.3	43.9
An important difficulty	13.3	13.9	17.1	13.1	13.4	12.1	11.6	12.7	12.6	12.3
Don't know	0.4	0.0	0.3	0.2	0.4	2.3	0.0	1.2	0.4	0.9
Missing	11.2	2.8	6.1	0.7	10.7	6.8	3.4	3.0	1.6	3.3
Acquiring information on tax laws and regulations is										
Not a difficulty	26.7	30.4	35.1	46.2	27.0	26.5	27.2	34.3	46.3	35.7
A moderate difficulty	46.8	47.2	35.3	46.0	46.7	43.2	51.0	47.0	43.5	45.9
An important difficulty	15.6	18.3	26.3	7.0	15.9	22.7	16.3	16.3	8.2	14.6
Don't know	0.1	1.3	0.0	0.8	0.1	2.3	1.4	0.6	1.6	1.4
Missing	10.8	2.8	3.3	0.2	10.2	5.3	4.1	1.8	0.4	2.4
Contacting tax administrations or tax officials is										
Not a difficulty	51.4	34.0	42.9	57.7	50.4	45.5	38.8	49.4	60.8	50.6
A moderate difficulty	17.8	42.6	31.9	30.4	19.4	24.2	41.5	32.5	29.0	31.6
An important difficulty	19.5	16.8	18.6	10.8	19.3	18.9	13.6	13.3	8.2	12.6
Don't know	0.5	4.4	0.2	0.6	0.7	5.3	2.7	1.8	0.8	2.3
Missing	10.8	2.3	6.4	0.5	10.3	6.1	3.4	3.0	1.2	3.0
Audits and litigation are										
Not a difficulty	22.7	28.2	23.8	23.2	23.0	24.2	32.0	28.9	27.5	28.1
A moderate difficulty	33.4	21.2	40.6	43.8	32.8	31.8	27.9	43.4	44.3	38.3
An important difficulty	23.3	39.4	31.0	28.9	24.3	25.0	28.6	24.1	22.4	24.6
Don't know	7.6	7.6	1.1	2.5	7.5	9.9	6.1	1.2	2.8	4.4
Missing	13.0	3.6	3.5	1.6	12.4	9.1	5.4	2.4	3.1	4.6
Responses	132	145	165	254	696	132	147	166	255	700

Question: "Complying with Company Tax legislation and procedures relating to domestic incomes may sometimes present difficulties. Some of these are listed below. Please give your opinion on each of them."

Note: Percentages in bold are different from zero at a 5% level of significance (see Annex D).

Most companies report only moderate difficulties for most issues. However, one can see in Table 3-1 that contacting tax administration and officials and audits and litigations are the two areas where the highest figures for "important difficulties" appear (respectively 19.3% and 24.3%). Concerning contacts with tax administrations and officials, this result contrasts with a relatively high percentage of companies indicating having no particular difficulties in their contacts with the administration. Future research could examine whether this result reflects national characteristics. Concerning audits and litigations, the figures seem to confirm that this is a difficult issue for companies, in particular large ones, in the domestic context.

3.2.2. *Company taxation issues related to income obtained in other EU Member States*

Of the 700 companies, only 165 reported having a subsidiary, a branch or a permanent establishment in another EU Member State. For those respondents, the same questions as those asked in the domestic context have been asked with respect to taxation of income originating in other EU Member States.

In what follows, we present first results for the SMEs, which regroup the micro, small and medium sized companies, and the large companies. In a second stage, responses obtained for these companies with regard to foreign-sourced income are compared to responses of the same companies with regard to domestic income.

It is important to note at this stage that only 51 companies that participated in the European Tax Survey are SMEs with a branch, a subsidiary or a permanent establishment in another Member State. Furthermore, a large proportion of the respondents originated in one Member State (see Annex C). Therefore, the data provided below concerning SMEs is not precise and may be unreliable. The main focus is thus placed on large companies here.

Question:

"Complying with Company Tax legislation and procedures relating to income in other EU Member States may sometimes present difficulties. Some of these are listed below. Please give your opinion on each of them."

The un-weighted estimates presented in Table 3-2 below indicate that 60 to 75% of companies in the sample, both SMEs and large companies, report at least some difficulties with the four issues considered, namely tax accounting and record keeping requirements, acquiring information on tax laws and regulations, contacting tax administrations or tax officials and audits and litigation. The most problematic issue for the SMEs in the sample is the acquisition of information on tax laws and regulations (75.0% report difficulties). For large companies, the highest figure is observed for audits and litigation in cross-border situations (70.8%).

Table 3-2 Opinions on issues related to foreign-sourced income

Un-weighted %	SMEs					Responses
	Not a difficulty	Moderate difficulty	Important difficulty	Don't know	missing	
Tax accounting/ record keeping	23.0	48.1	17.3	3.9	7.7	52
Acquiring information on tax laws and regulations	15.4	51.9	23.1	1.9	7.7	52
Contacting tax administrations or tax officials	19.2	48.1	21.1	3.9	7.7	52
Audits and litigation	21.2	48.1	15.4	5.8	9.6	52

	Large companies					
Un-weighted %	Not a difficulty	Moderate difficulty	Important difficulty	Don't know	missing	Responses
Tax accounting/ record keeping	27.4	51.3	12.4	1.8	7.1	113
Acquiring information on tax laws and regulations	24.8	53.1	13.3	1.8	7.1	113
Contacting tax administrations or tax officials	20.4	51.3	15.0	3.5	9.7	113
Audits and litigation	12.4	46.9	23.9	4.4	12.4	113

	Large companies					
Weighted %	Not a difficulty	Moderate difficulty	Important difficulty	Don't know	missing	Responses
Tax accounting/ record keeping	28.6	51.9	12.2	2.9	4.4	113
Acquiring information on tax laws and regulations	30.1	54.2	9.3	2.0	4.4	113
Contacting tax administrations or tax officials	26.3	54.4	9.1	3.8	6.5	113
Audits and litigation	9.8	48.1	27.9	5.2	9.1	113

Note: Percentages in bold are different from zero at a 5% level of significance (see Annex D).

The second part of Table 3-2 presents the detailed weighted results for large companies only (it was not possible to provide meaningful detailed weighted data for SMEs). The results are fairly consistent with the results obtained for un-weighted data. It is interesting to note that audits and litigations is by far the issue for which the estimated percentage of large firms indicating having important difficulties is highest (32.1%).

Comparison and overview:

These results can be compared with results obtained in the domestic context from the same sample of companies with subsidiaries, branches or permanent establishments in other EU countries.

Table 3-3 indicates that acquiring tax information and contacting tax administrations is more difficult with regard to foreign-sourced income than to domestic income. The results seem to reflect the fact that the contact with foreign administration is particularly more difficult than the contact with domestic administrations. This is understandable as it is more generally accepted that such "foreign" contacts might be more difficult.

The table also highlights that tax accounting and record keeping requirements cause more difficulties to large companies with regard to domestic income than concerning foreign-sourced income (the results for SMEs are unreliable due to the low number of observations). This does not come as a great surprise either, as the number of elements to report and keep track of is in principle much lower with regard to foreign-sourced income. The SMEs and the large companies have also lower difficulties due

to audits and litigations for foreign-sourced income. This probably reflects the focus of national tax administrations on domestic operations and, again, the limited number of operations related to foreign-sourced income.

Table 3-3 Opinions with respect to foreign-sourced income - comparison with domestic results (companies with a subsidiary, a branch or a permanent establishment in another EU state)

% indicating a difficulty (weighted results)	SMEs			Large companies		
	Domestic income	Foreign income	Comparison (+ indicate more difficulty with foreign income)	Domestic income	Foreign income	Comparison (+ indicate more difficulty with foreign income)
Tax accounting record keeping	22.9	88.4	+++	74.6	64.1	–
Acquiring information	94.8	95.2	+	62.4	63.5	+
Contacting the administration	77.5	92.6	++	38.9	63.5	++
Audits and litigations	89.0	85.6	–	83.3	76.0	–
Responses	51	51		113	113	

Note: Percentages in bold are different from zero at a 5% level of significance (see Annex D).

Box 3-2 Results obtained in other qualitative surveys

A survey on institutional obstacles for doing business by the World Bank shows that companies in industrial countries perceive tax regulations and high taxes as the most important obstacles to doing business (see Brunetti, Kisunko and Weder (1998)).

UNICE (1995) conducted a survey of 2100 companies (80% SMEs) to investigate how regulatory burdens can be reduced for companies. A majority of companies was found to believe there are shortcomings of tax and other administrative regulations. Companies identified the increase of administrative costs and the diversion of management time as factors reducing their competitiveness. In particular, the provision of statistics, collection of direct and indirect taxes, the administration of sickness schemes and the calculation and payment of corporate taxes were identified as operational aspects hampering competitiveness of companies.

OECD (2001) present survey results of the opinion of SMEs on administrative and regulatory burdens. Environmental, employment and tax regulations are considered. On tax regulations their findings indicate that SMEs disagree with the effectiveness of information provision by the responsible agencies on some aspects. A majority of companies disagrees with tax agencies being easy to contact. In addition, most of companies feel that not everybody in a tax agency has the same view on tax regulations. As concerns obtaining decisions or permissions on tax regulations a majority of SMEs voices disagreement with the consistency, predictability, transparency and speed of the decision-taking process.

3.2.3. *Opinions on specific issues related to corporate taxation*

In addition to questions related to complying with taxes with regard to domestic income or to income arising in other EU Member States, a number of additional questions related to specific tax obstacles have been asked to the respondents with a subsidiary, a branch or a permanent establishment in another EU Member State. Results are provided for SMEs and large companies with a subsidiary, a branch or a permanent establishment in another EU Member State.

Question:

"In the course of your business how important an obstacle to your cross-border activity (trade, investment) in the European Union is (i) the absence of cross-border loss compensation, (ii) double taxation on repatriated profits and other income from subsidiaries and branches (eg dividends, interest, royalties), (iii) transfer pricing, (iv) taxation of mergers and acquisitions and (v) the cost of dealing with different national tax systems"

Table 3-4 below indicates the weighted percentages of companies that find the issues important. The percentages obtained provide a useful indication as to the specific concerns for companies. They suggest in particular that, with regard to foreign-sourced income, the main concern to companies could be problems related to transfer pricing. For both SMEs and large companies, figures for transfer pricing are highest (respectively 91.3% and 82.8% of companies indicating that the issue is important). The weighted results also highlight that more than 80% of SMEs and large companies consider the costs of dealing with different tax systems as important.

Table 3-4 Opinions on foreign-sourced income (weighted results)

% indicating a difficulty	SMEs	Large
The absence of cross-border loss compensation	22.9	64.3
Double taxation on repatriated profits	24.3	71.2
Transfer Pricing	91.3	82.8
Taxation of mergers and acquisitions	15.7	51.1
Costs of dealing with different tax systems	89.6	80.8
Responses	51	113

Note: Percentages in bold are different from zero at a 5% level of significance (see Annex D).

Interestingly, based on responses obtained from the participants to the European Tax Survey, one can see that fewer companies (only 51.1% of large companies) indicate that the taxation of mergers and acquisitions is important. This could indicate that fewer companies have problems there. However, a closer look at the results shows that the percentage of "don't know/missing" for this question is higher than for the other issues. This suggests that a proportion of companies do not really have experience with the issue. In particular, it is likely that this type of operations usually mainly concerns large companies with specific characteristics. Actually, if one recalculates the percentages above without including "missing" responses, the

percentage of companies considering the issue of mergers and acquisitions as important is higher than percentages observed for the other issues. This suggests that, for companies concerned, cross-border mergers and acquisitions still constitute important problems, despite the existence of rules at EU level (the Council Directive on mergers and acquisitions 90/434/EEC). Further discussions on this important issue can be found in section 3.4.3 below.

3.2.4. Transfer Pricing

The analysis above highlights the importance of transfer pricing for many companies. It also confirms an important result of the statistical analysis undertaken in section 2-5 of Chapter 2, namely that companies involved in transfer pricing investigations have higher compliance costs even when taking into account other company characteristics. This does not come as a surprise since it is often argued that this is one of the main tax concerns of EU multinational companies and led to the creation of the Joint Transfer Pricing Forum (see Box 3-3 below).

Therefore, in the context of the European Tax Survey, particular attention was paid to this issue. Specific questions were asked to companies which had their cross-border intra-group transactions ('transfer pricing') examined in the past five years. In total 110 out of the 700 companies provided responses. Three questions related to transfer pricing were asked. The tables below present the results for the 74 large companies in this sample.

The weighted results in Table 3-5 underline two main problems. Whereas 81.9% of large companies which had their cross-border transfer pricing examined in the past five years have difficulties dealing with documentation requirements linked to transfer pricing, almost the same percentage of companies, 79.9%, have difficulties dealing with the risk of double taxation. A lower percentage of companies appear to have difficulties with regard to dealing with procedures for dispute resolution. However, the question is not applicable to 37.8% of companies. In practice, it may well be that companies are either not confronted to the issue of dispute resolution or simply choose not to engage in such procedures and accept double taxation rather than becoming involved in long and complex dispute resolution procedures, whose outcome is uncertain. Further research should examine more closely the link between difficulties encountered and actual cases of dispute resolution.

Table 3-5 Opinions on transfer pricing (large companies)

Un-weighted % (large firms)	Not a difficulty	A difficulty	Don't know/Missing	Responses
Regarding transfer pricing, dealing with documentation requirements is	10.8	79.7	9.5	74
Regarding transfer pricing, dealing with the risk of double taxation is	12.2	77.0	10.8	74
Regarding transfer pricing, dealing with procedures for dispute resolution is	5.4	56.8	37.8	74

Weighted % (large firms)	Not a difficulty	A difficulty	Don't know/Missing	Responses
Regarding transfer pricing, dealing with documentation requirements is	12.1	81.9	6.0	73
Regarding transfer pricing, dealing with the risk of double taxation is	12.3	79.9	7.8	73
Regarding transfer pricing, dealing with procedures for dispute resolution is	4.2	59.9	35.9	73

Note: Percentages in bold are different from zero at a 5% level of significance (see Annex D).

Box 3-3 The Joint Transfer Pricing Forum

Following its Communication “Towards an Internal Market without tax obstacles – A strategy for providing companies with a consolidated corporate tax base for their EU-wide activities” COM (2001) 582 of 23 October 2001 the EU Commission set up the EU Joint Transfer Pricing Forum (hereafter JTPF). The Forum now has 35 Members, one expert for each Member State and 10 experts from business. Representatives from EU candidate countries and the OECD are observers.

The JTPF aims to identify possible non-legislative improvements to the practical problems related to transfer pricing in the Internal Market and the implementation of the EU Arbitration Convention. Improvements of the existing dispute resolution procedures, e.g. expediting the procedures and enhanced transparency, and a possible EU-wide standardisation of transfer pricing documentation requirements were given the highest priority. The JTPF also examined the issue of interest charges for back taxes and interest on tax refunds and penalties. Due to the complexity of the above issues and specially the potential impact on domestic legislation, the JTPF decided, however, to defer more in-depth discussions on this to a later stage.

The JTPF also identified that the majority of Member States do not have rules providing for the suspension of tax collection during cross-border dispute resolution procedures which can create an additional financial burden for companies facing double taxation.

In December 2003 the JTPF decided to submit to the Commission a report on its activities so far and to propose a Code of Conduct on procedural issues related to the practical functioning of the Arbitration Convention and certain related issues of mutual agreement procedures under double tax treaties between Member States. A recommendation to expand the suspension of tax collection during cross-border dispute resolution procedures under the same conditions as the internal procedures was also adopted by the Forum. The Commission has issued a Communication to the Council on the JTPF's report and the proposed Code of Conduct (see COM(2004)297 of 23 April 2004).

The JTPF continues its work through 2004 and expects to accomplish its project on EU-wide documentation. It also envisages starting discussions on preventive measures to avoid double taxation by the end of 2004.

3.3. VAT

This section focuses on qualitative questions related to compliance costs for VAT. The approach followed here is similar to the one of the previous section. Firstly, responses to the questions on issues linked to domestic obligations in the area of VAT are examined. Responses on issues related to VAT obligations in other EU Member States are presented next. A comparison is then made in order to highlight possible specific problems arising when companies are engaged in cross-border activities. This analysis is completed by looking at the situation of companies registered in another Member State for VAT purposes but without a permanent establishment in that country. This section ends with questions on specific VAT issues.

The previous chapter highlighted that VAT compliance costs increase with company size, as well as the degree of cross-border activity (measured by the number of subsidiaries abroad). Furthermore, companies with VAT obligations in another EU Member State without having a permanent establishment that also incur VAT on inputs abroad have higher VAT compliance costs than purely domestic companies. The analysis of the opinions of companies on VAT issues will allow for a better insight of the results obtained in Chapter 2.

Before turning to the results of the qualitative analysis, a caveat needs to be mentioned. Similar to the previous section, comparisons are made between results obtained for SMEs and large companies. In the case of issues related to VAT, this raises a specific problem. The size of companies in the context of the European Business Test Panel was determined on the basis of their number of employees. No other variable was used to separate micro, small, medium and large companies. However, in practice, relatively small companies can have extended activities measured in terms of, for instance, turnover. This classification could constitute a problem for the analysis as a number of tax obligations linked to VAT depend on the size of companies as measured by turnover in some Member States. However, as Box 3-4 below indicates, there is a strong correlation between the size of companies

measured by the number of employees and their turnover in the European Tax Survey.

Box 3-4 Sales and company size in the European Tax Survey

In the European Tax Survey company size is measured in terms of employees. But when it comes to VAT regulation it is often sales that determine which requirements have to be fulfilled by companies. Therefore, it is useful to examine the link between sales and the company size classes defined in the European Business Test Panel.

The table below shows the distribution of sales by deciles within each company size class. For example, the table indicates that 20% of the micro companies reported sales that lie below 108.000 euros, while 30% of micro companies reported sales below 282.000 euros.

Sales Distribution by Company Size (€1.000)

Deciles	Micro	Small	Medium	Large
10%	52	518	2,524	15,586
20%	108	982	5,422	34,541
30%	282	1,477	7,506	60,134
40%	444	1,850	12,133	91,042
50% (median)	734	2,750	16,354	148,500
60%	1,132	3,788	21,808	258,165
70%	1,902	5,111	30,000	655,835
80%	5,393	7,785	4,460	1,695,531
90%	44,839	13,868	101,843	4,903,600
100%	6,836,200	3,500,000	1,115,151	2,604,326,912
Average	131,922	32,320	55,813	13,658,005
Observations	116	135	147	230

Note: Observations with zero sales are not included. In addition, nine observations are excluded as the respondent's remarks suggested that there are problems with reported sales.

The sales reported for each decile increase across company size classes. For instance, for the second decile, the amounts indicated are €108.000, 982.000, 5.422.000 and 34.541.000 for micro, small, medium and large companies, respectively. A similar pattern can be observed for each decile, except the last one, for which micro companies present substantially larger sales than small companies.

Overall, the average sales are higher for large companies compared to medium companies. In turn the average sales are higher for medium companies compared to small companies. However, the average sales are lower for small companies compared to micro companies. This last result is due to a small number of micro companies with relatively large sales.

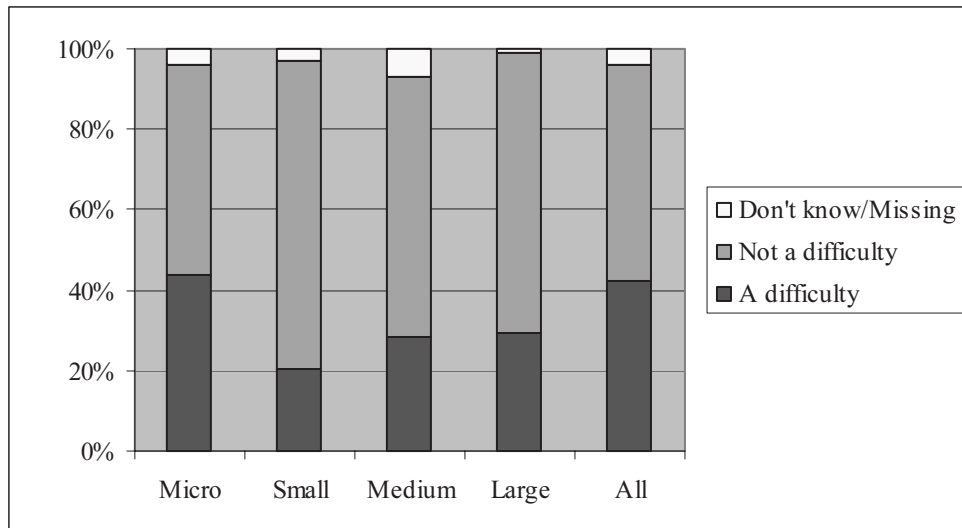
Therefore, it can be reasonably concluded that company size classes retained for the European Business Test Panel based on the number of employees reflect to a large extent company sizes based on sales. The only exception could be micro companies, for which a number of companies have relatively large sales.

3.3.1. VAT issues related to domestic activities

Question:

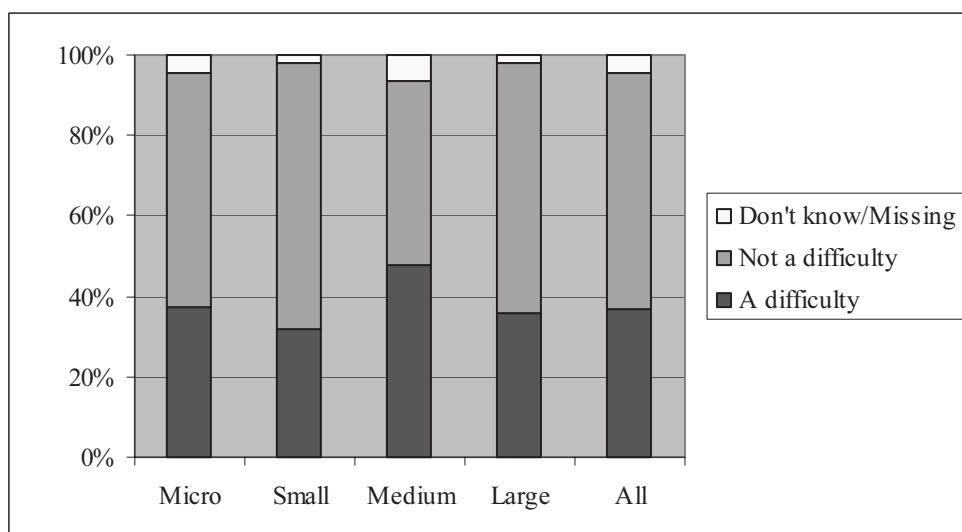
"Complying with domestic VAT obligations may sometimes present difficulties. Some of these are listed below. Please give your opinion on each of them."

Graph 3-6 Opinions on identification and registration (weighted results)



The weighted results shown in Graph 3-6 indicate that 53.8% of all companies do not have particular difficulties with regard to identification and registration²⁹. Figures appear particularly high for small companies (76.3%), but much lower for micro companies (52.3%).

Graph 3-7 Opinions on the frequency of VAT tax returns and listings (weighted results)

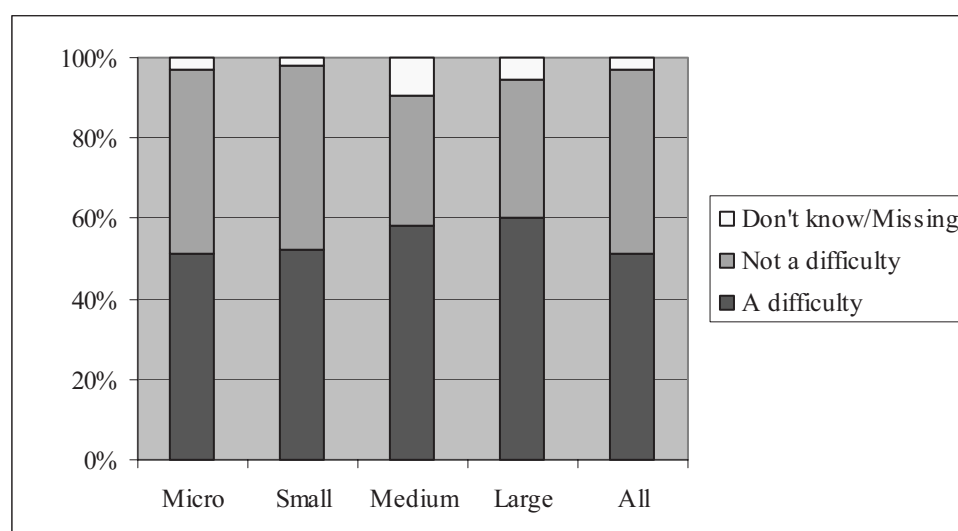


²⁹

The figures used for this graph and the following ones can be found in Table 3-6 below.

The Graph 3-7 above shows that 58.5% of all companies find that the frequency of VAT returns and listings does not constitute a difficulty in the domestic context. Figures vary between 45.6% for medium companies and 66.3% for small companies. As the frequency requirements mostly depend on the turnover of companies, one would expect the reported difficulties to increase with the size of companies. At the same time, for two companies of different size submitted to equivalent requirements, one would expect the larger one to report less difficulties since it would have a better internal capacity to cope with administrative obligations, *ceteris paribus*. The results presented above could confirm these expectations. Most micro and small firms probably benefit from a regime of annual returns and listings, while most medium and large companies probably face more constraining rules. In that context, smaller difficulties can be expected for small and large companies compared to micro and medium companies, respectively. However, further research would be necessary to confirm the validity of this hypothesis.

Graph 3-8 Opinions on the complexity of VAT tax returns and listings (weighted results)



The weighted estimates indicate that 51.2% of companies have difficulties with regard to VAT returns and listings (see Graph 3-8). Furthermore, difficulties increase with the size of companies. Whereas 51.0% of micro companies indicate that the complexity of VAT systems implies difficulties, figures are 52.3%, 58.2% and 60.1% for small, medium and large companies respectively. This result is not surprising, because the requirements imposed on companies, as well as the variety and difficulty of tax treatment often increase with company size, and so do the difficulties of legal questions (see Box 3-5 below).

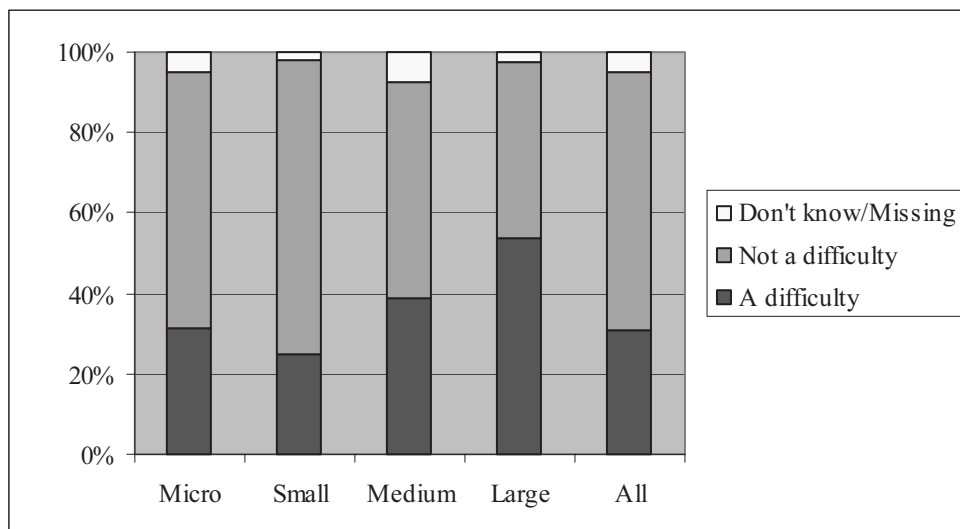
Box 3-5 VAT requirements and the size of companies

VAT requirements imposed on companies vary in the different Member States. This is due to the fact that the Sixth VAT Directive (77/388/EC) only lays down some minimum requirements applicable to all Member States but most of the VAT rules are national rules. Detailed information about these rules can be found on the European Commission Taxation and Customs Union Directorate-general website (VAT obligations report – see http://europa.eu.int/comm/taxation_customs/taxation/vatindex_en.htm, click on "VAT systems in the European Union").

Most of the Member States have implemented specific rules for very small or small companies (usually corresponding to micro or small companies in the European Tax Survey). Thresholds have also been implemented under which no VAT obligation at all is imposed. These thresholds vary a lot and can reach up to €86 000 of VAT turnover.

Besides the biggest companies are also the ones faced with the most important variety of situations and VAT treatments (different rates or exemptions...). One could therefore expect that the smaller a company is, the less difficulty it has in relation to VAT obligations.

Graph 3-9 Opinions on invoicing requirements (weighted results)



Invoicing requirements do not lead to difficulties for a majority of companies as can be seen in Graph 3-9. The weighted estimates highlight that 64.2% of companies do not find it a difficulty to cope with these obligations. However, it should be noted that 53.6% of large companies indicate invoicing requirement as a difficulty. This is a much higher figure than the one obtained for small companies, for instance (25.1%). Here the same conclusion as in Graph 3-8 can probably be drawn: the variety of invoicing rules, which have to be followed, increases with the variety of VAT treatment. Since the new invoicing directive (Directive 2001/115/EC) came into force on the 1st January 2004, some very complex and burdensome rules in some Member States could have disappeared since the European Tax Survey was completed (see Box 3-6).

Box 3-6 VAT invoicing requirements

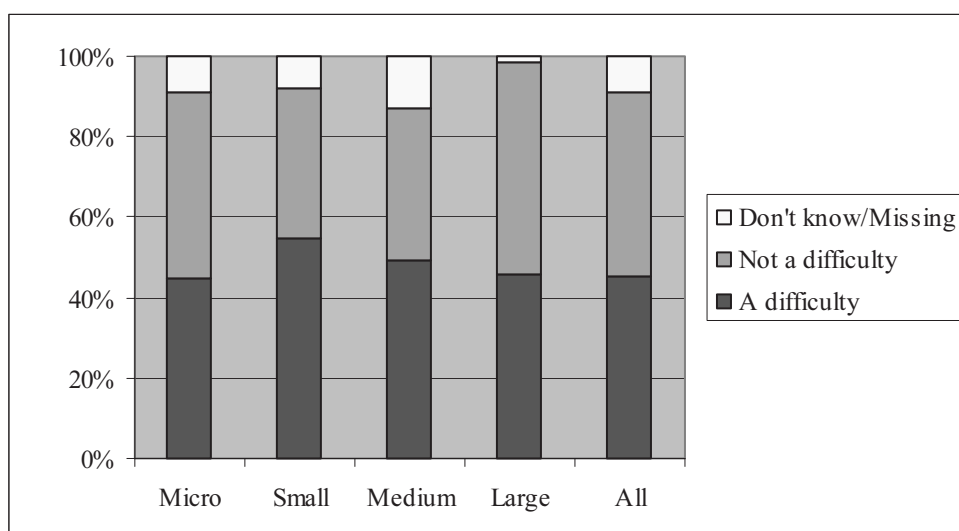
VAT invoicing requirements have been dramatically simplified due to the entry into force of Directive 2001/115/EC.

This Directive lays down new harmonised rules on :

- what details an invoice should contain,
- who can issue an invoice on behalf of the supplier,
- which medium (paper or electronic) it can be issued,
- how (paper or electronic medium) and where (in the country or outside the country) it should be stored.

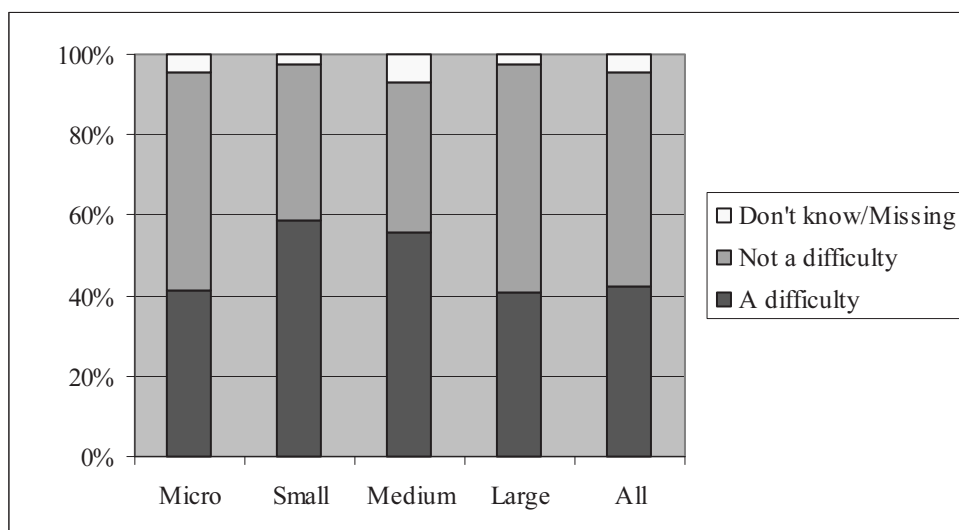
This Directive had to be implemented by the Member States by the end of 2003. The present survey however reflects the situation before the implementation of this directive.

Graph 3-10 Opinions on repayment and refund requirements (weighted results)



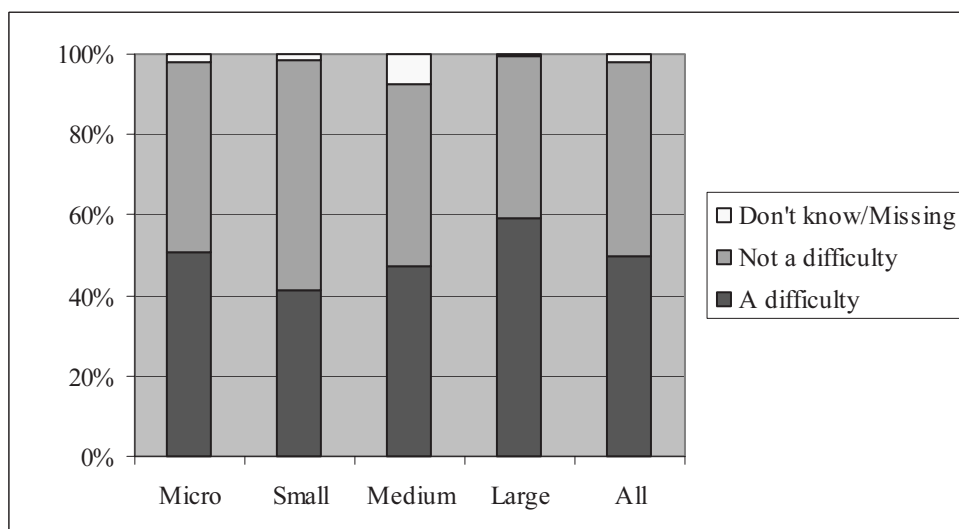
The weighted results concerning repayment and refund requirements in the domestic context are rather balanced (see Graph 3-10). While 45.2% of companies are estimated to have difficulties, 45.8% do not have particular difficulties in this respect. However, a slightly higher figure (54.5%) can be observed for small firms. One possible explanation is that the impact of long repayment time can be more problematic for the cash flow of smaller firms. However, the result obtained for micro firms does not seem fully consistent with that interpretation, but this may be due to the fact that some of those companies do not charge VAT at all because they benefit from a flat-rate scheme. Such a scheme allows traders, in special cases (e.g. farming), to choose between the "normal" taxation rules and simpler, flat-rate, rules.

Graph 3-11 Opinions on accessing tax information and contacting tax officials (weighted results)



The weighted figures in Graph 3-11 indicate that 53.4% of companies do not find it difficult to access to tax information and to contact tax officials regarding domestic VAT obligations. However, differences can be observed between categories of companies. 58.7% and 55.6% of small and medium-sized companies, respectively, indicate having difficulties in this respect. This is probably due to the fact that smaller companies need as various and detailed information as large companies, but do not employ tax specialists, who are familiar with the subject.

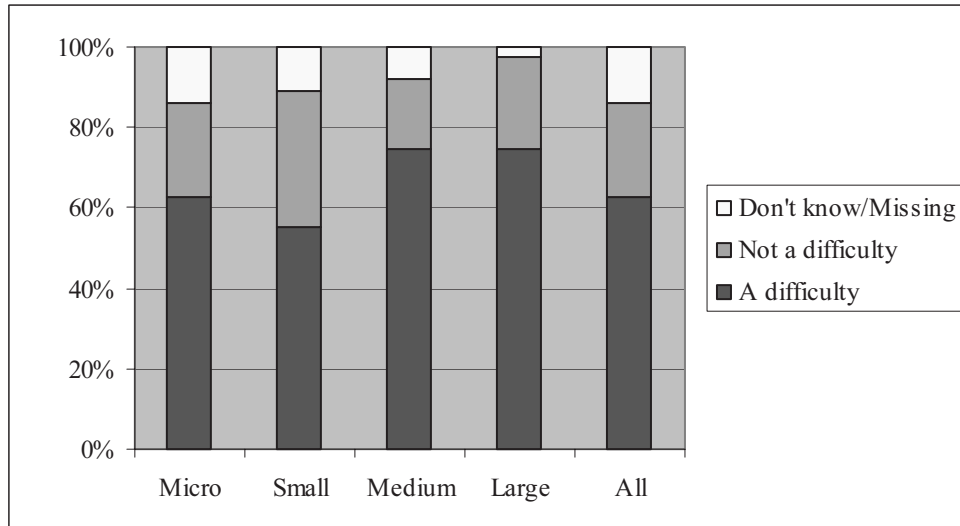
Graph 3-12 Opinions on record keeping requirements (weighted results)



Concerning record keeping requirements, opinions vary substantially depending on the size of companies. The weighted results show that 59.2% of large companies have difficulties. This contrasts with significantly lower figures for medium (47.4%) and small (41.4%) companies. The results also point at difficulties for 50.6% of micro companies. A part of the problems resulting from the variety of rules and requirements, for instance with regard to e-record keeping, could have disappeared

since 1st January 2004 with the entry into force of the invoicing directive (see Box 3-6 above). Future research could usefully assess the impact of this directive on opinions of companies with regard to record keeping requirements.

Graph 3-13 Opinions on audits and litigation (weighted results)



The weighted estimates indicate that 62.6% of all companies have difficulties with regard to audits and litigation related to domestic VAT obligations (see Graph 3-13). In fact the results show that close to three quarter of medium and large companies have difficulties in this area. It should also be noted that the percentage of "don't know/missing" responses decrease with the company size, which could reflect the fact that larger firms are more likely to be confronted to problems linked to audits and eventual litigations. Overall, the responses suggest that larger firms are more likely to face problems related to audits and litigations, which in turn require specific resources and involve additional difficulties.

Comparison and overview:

Table 3-6 below provides the detailed disaggregated results underlying the above graphs. These permit a more precise examination of results, and in particular to identify where companies encounter important difficulties, and a comparison of opinions for different issues.

It is worth noting that the opinions of companies differ significantly between issues. In particular, whereas only few companies underscore "identification and registration" or "the frequency of VAT tax returns and listings" as important difficulties, much higher percentages can be observed in the other areas. Based on weighted results obtained from the responses to the European Tax Survey, it appears that audits and litigations are qualified as important difficulties by 20.4% of all companies. It is also interesting to note the differing opinions of micro and large companies concerning invoicing requirements (2.6% vs. 12.6% indicating an important difficulty). This is coherent with the fact that requirements imposed on larger companies are more stringent than for smaller companies.

Table 3-6 Opinions on domestic VAT issues

Company size	Weighted percentages					Un-weighted (sample) percentages				
	Micro	Small	Medium	Large	All	Micro	Small	Medium	Large	All
Identification and registration										
Not a difficulty	52.3	76.3	64.9	69.3	53.8	58.3	70.8	60.2	67.8	64.9
A moderate difficulty	38.6	20.1	25.7	25.8	37.4	26.5	21.8	31.3	26.7	26.7
An important difficulty	5.1	0.4	2.5	3.7	4.8	4.6	1.4	5.4	3.5	3.7
Don't know	0.9	0.3	0.2	1.1	0.8	3.0	1.4	0.6	1.6	1.6
Missing	3.1	2.9	6.7	0.2	3.1	7.6	4.8	2.4	0.4	3.1
The frequency of VAT tax returns and listings										
Not a difficulty	58.2	66.3	45.6	62.0	58.5	49.2	63.3	54.2	62.8	58.3
A moderate difficulty	34.7	31.4	36.0	31.6	34.6	37.1	30.6	33.7	31.0	32.7
An important difficulty	2.5	0.6	11.7	4.4	2.5	5.3	2.7	9.6	3.5	5.1
Don't know	1.8	0.0	0.3	0.9	1.6	2.3	0.0	0.6	1.2	1.0
Missing	2.8	1.8	6.5	1.1	2.8	6.1	3.4	1.8	1.6	2.9
Complexity of VAT tax returns and listings										
Not a difficulty	45.8	45.7	32.2	34.3	45.7	40.9	42.2	36.1	41.2	40.1
A moderate difficulty	34.8	43.1	46.8	45.1	35.4	37.1	42.9	41.6	40.0	40.4
An important difficulty	16.2	9.2	11.3	14.9	15.8	12.1	8.8	17.5	14.1	13.4
Don't know	0.3	0.1	0.0	0.8	0.3	3.0	0.7	0.0	0.8	1.0
Missing	2.8	2.0	9.7	4.8	2.8	6.8	5.4	4.8	3.9	5.0
Invoicing requirements										
Not a difficulty	63.8	72.7	53.7	44.1	64.2	59.9	72.8	59.0	47.5	57.9
A moderate difficulty	28.7	16.0	29.5	40.9	28.0	25.0	19.7	31.3	40.8	31.1
An important difficulty	2.6	9.1	9.3	12.6	3.0	4.6	3.4	6.6	9.4	6.6
Don't know	1.6	0.0	0.2	0.2	1.5	2.3	0.0	0.6	0.8	0.9
Missing	3.3	2.2	7.3	2.1	3.3	8.3	4.1	2.4	1.6	3.6
Repayment and refund requirements										
Not a difficulty	46.3	37.6	37.8	52.5	45.8	35.6	36.7	47.0	50.6	44.0
A moderate difficulty	35.1	43.3	31.2	34.0	35.5	33.3	38.1	30.1	36.1	34.6
An important difficulty	9.5	11.2	18.0	11.8	9.7	13.6	13.6	15.1	11.0	13.0
Don't know	3.7	5.8	4.8	0.1	3.8	5.3	6.1	3.6	0.4	3.3
Missing	5.3	2.1	8.1	1.6	5.2	12.1	5.4	4.2	2.0	5.1
Accessing tax information and contacting tax officials										
Not a difficulty	54.4	38.6	37.6	56.8	53.4	39.4	35.4	44.0	55.7	45.6
A moderate difficulty	23.2	37.3	34.2	29.9	24.1	28.0	46.9	38.0	32.9	36.1
An important difficulty	18.0	21.4	21.4	10.7	18.2	17.4	12.9	15.1	8.6	12.7
Don't know	3.1	0.9	0.3	1.8	3.0	6.1	1.4	1.2	1.6	2.3
Missing	1.3	1.8	6.5	0.8	1.4	9.1	3.4	1.8	1.2	3.3
Record keeping requirements										
Not a difficulty	47.5	56.9	45.4	40.5	48.0	43.9	49.7	48.8	42.8	45.9
A moderate difficulty	35.3	34.5	34.8	45.4	35.2	38.6	39.5	35.5	44.3	40.1
An important difficulty	15.3	6.9	12.5	13.8	14.8	10.6	8.2	13.3	12.2	11.3
Don't know	0.2	0.0	0.8	0.1	0.2	2.3	0.0	0.6	0.4	0.7
Missing	1.8	1.7	6.5	0.2	1.8	4.6	2.7	1.8	0.4	2.0
Audits and litigation										
Not a difficulty	23.1	33.7	17.4	23.0	23.6	25.0	32.7	29.5	27.5	28.6
A moderate difficulty	42.7	33.7	46.7	49.9	42.2	33.3	36.7	44.0	46.3	41.3
An important difficulty	20.2	21.7	28.0	24.7	20.4	18.9	19.1	20.5	21.6	20.3
Don't know	7.9	8.6	1.2	1.6	7.9	9.9	6.8	2.4	2.8	4.9
Missing	6.1	2.2	6.8	0.8	5.9	12.9	4.8	3.6	2.0	5.0
Responses	132	145	165	254	696	132	147	166	255	700

Question: "Complying with domestic VAT obligations may sometimes present difficulties. Some of these are listed below. Please give your opinion on each of them". Note : Percentages in bold are different from zero at a 5% level of significance (see Annex D).

3.3.2. *VAT issues in other EU Member States*

In order to highlight possible issues in the VAT area arising from cross-border activities, additional questions were asked to the 165 respondents having a subsidiary, a branch or a permanent establishment in another EU Member State. For those respondents, the same questions as previously have been asked with respect to VAT activities in other EU Member States. In what follows the results of these questions are presented for the SMEs and large companies.

Before turning to the results for these questions, it should be noted that having a permanent establishment implies having persons in charge of VAT obligations abroad. In most cases, one expects this to limit difficulties related, for instance, to language or specific cultural differences. Furthermore, as VAT rules are largely harmonised at EU level, one should expect percentages obtained for the various questions to be fairly similar to the ones observed in the domestic context. In addition, the limited number of SMEs with a branch, a subsidiary or a permanent establishment included in the European Business Test Panel does not allow producing accurate information for that type of companies. The main focus of this section is therefore placed on large companies.

Question:

"Complying with VAT obligations in other Member State(s) where you have a permanent establishment may present a number of problems. Some of these are listed below. Please give your opinion on each of them."

Table 3-7 below presents first the un-weighted data for both SMEs and large companies. The weighted data is presented next for the large companies only (there were too few responses for SMEs to produce meaningful weighted estimates). The un-weighted results underline the existence of some particularly problematic issues for the sample of companies in the European Business Test Panel. For both SMEs and large companies the issue most generally recognized as leading to difficulties is the audits and litigations (59.6% and 54.8% respectively) indicating a moderate or an important difficulty.

Table 3-7 Opinions VAT obligations in other Member States

Un-weighted %	SMEs					Responses
	Not a difficulty	Moderate difficulty	Important difficulty	Don't know	missing	
Identification and registration	38.5	38.5	9.6	1.9	11.5	52
The frequency of VAT tax returns and listings	30.8	46.2	3.9	7.7	11.5	52
The complexity of VAT tax returns and listings	21.2	38.5	13.4	7.7	19.2	52
Invoicing requirements	42.3	36.5	1.9	7.7	11.5	52
Repayment and refund requirements	26.9	28.9	19.2	9.6	15.4	52
Accessing tax information and contacting tax officials	26.9	36.5	15.4	9.6	11.5	52
Record keeping requirements	34.6	38.5	9.6	3.9	13.5	52
Audits and litigation	19.2	48.1	11.5	5.8	15.4	52

Un-weighted %	Large companies					Responses
	Not a difficulty	Moderate difficulty	Important difficulty	Don't know	missing	
Identification and registration	33.6	29.2	15.0	4.4	17.7	113
The frequency of VAT tax returns and listings	36.3	35.4	6.2	4.4	17.7	113
The complexity of VAT tax returns and listings	19.5	28.3	19.5	3.5	29.2	113
Invoicing requirements	22.1	41.6	15.0	2.7	18.6	113
Repayment and refund requirements	15.9	37.2	23.9	4.4	18.6	113
Accessing tax information and contacting tax officials	16.8	42.5	16.8	4.4	19.5	113
Record keeping requirements	22.1	41.6	15.0	3.5	17.7	113
Audits and litigation	17.7	32.7	22.1	8.0	19.5	113

	Large companies					
weighted %	Not a difficulty	Moderate difficulty	Important difficulty	Don't know	missing	Responses
Identification and registration	36.0	28.4	14.1	2.2	19.3	113
The frequency of VAT tax returns and listings	29.4	41.1	6.9	3.3	19.3	113
The complexity of VAT tax returns and listings	19.7	32.4	19.9	3.4	24.5	113
Invoicing requirements	23.8	37.2	18.7	0.9	19.4	113
Repayment and refund requirements	14.0	39.2	22.9	3.3	20.6	113
Accessing tax information and contacting tax officials	22.0	43.0	13.5	2.9	18.7	113
Record keeping requirements	22.6	39.7	16.6	2.4	18.7	113
Audits and litigation	16.4	28.5	29.2	7.2	18.6	113

Note: Percentages in bold are different from zero at a 5% level of significance (see Annex D).

The weighted estimates for large companies presented in Table 3-7 provide slightly different results than the un-weighted data. This time repayment and refund requirements appear as the issue leading to difficulties in most cases (62.1% of moderate or important difficulties), at a similar level as audits and litigations (57.8%). Interestingly, these two issues are also the ones where the highest figures are obtained for important difficulties (22.9% and 29.2%, respectively).

Comparison and overview:

In order to compare difficulties arising with regard to domestic VAT obligations and foreign (EU) VAT obligations, the following Table 3-8 presents the figures for the same 165 respondents (having a subsidiary, a branch or a permanent establishment in another EU Member State), this time in the domestic context.

Concerning large companies, in five areas, the frequency and the complexity of VAT returns and listings, invoice and record keeping requirements and audits and litigations, a lower percentage of companies indicate having difficulties in the foreign context than in the domestic context. An opposite result is found for identification and registration, for repayment and refund requirements and for accessing tax information and contacting tax officials. Concerning SMEs, the weighted estimates are unfortunately not significant due to the limited number of responses obtained and it is therefore difficult to draw conclusions from the data below.

Overall, these results do not indicate *systematic* problems in the area of VAT linked to cross-border activities. For companies having a permanent establishment in another Member State it is not a surprising outcome that difficulties with VAT obligations are more or less the same than at home. Furthermore, for companies with a permanent establishment in another EU Member State the foreign obligations are also of a "domestic" nature. Their employees are used to dealing with the foreign rules and the language or cultural factors presumably do not play a very important role.

Table 3-8 Opinions on VAT obligations in the domestic and foreign situation

	SMEs			Large companies		
% indicating a difficulty (weighted results)	Domestic VAT obligations	VAT obligations in other MS	Comparison (+ indicate more difficulty abroad)	Domestic VAT obligations	VAT obligations in other MS	Comparison (+ indicate more difficulty abroad)
Identification and registration	8.3	16.6	+	30.2	42.5	++
The frequency of VAT tax returns and listings	7.4	8.7	+	43.6	48.0	–
The complexity of VAT tax returns and listings	17.0	12.6	–	67.6	52.3	—
Invoicing requirements	9.0	13.8	+	61.0	55.9	–
Repayment and refund requirements	17.8	14.4	–	45.6	62.1	++
Accessing tax information and contacting tax officials	18.4	15.5	–	39.0	56.4	++
Record keeping requirements	13.4	11.1	–	73.9	56.3	—
Audits and litigation	20.5	18.0	–	82.9	57.8	—
Responses	51	51		113	113	

Note: Percentages in bold are different from zero at a 5% level of significance (see Annex D).

Nevertheless, where important differences between the domestic situation and the foreign situation are observed, this may indicate the existence of specific problems and, ultimately, the need for policy intervention. For instance, the opinions on the issue of identification and registration suggest that companies face more difficulties abroad than they do in the domestic context. Besides, large companies are confronted to specific difficulties in foreign EU Member States on repayment and refund requirements and for accessing tax information and contacting tax officials. Last, opinions received on tax returns and listings and record keeping requirements and on audits and litigations suggest that dealing with domestic VAT requirements is more difficult than with foreign requirements. This again raises questions as to how compliance costs could be reduced.

3.3.3. *VAT issues for firms registered in a Member State where they don't have a permanent establishment*

In order to have a clearer picture of the consequences of VAT obligations for companies, the situation of companies registered in a Member State for VAT purposes without having a permanent establishment has also been examined. This specific situation concerns 97 of the 700 respondents to the questionnaire. Due to the

limited number of replies for SMEs, only estimates based on responses from large companies (60) are presented below.

In what follows, tables present first the detailed opinions of large companies with regard to VAT obligations in other EU Member States. The results are then compared to responses provided by the same companies in the domestic context.

Question:

"Complying with VAT obligations in another EU Member State(s) where you do not have a permanent establishment can give rise to problems. Some of these are listed below. Please give your opinion on each of them."

Table 3-9 Opinions of large companies registered in a Member State where they don't have a PE

Un-weighted %	Not a difficulty	A difficulty	Don't know/Missing	Responses
Identification and registration	25.0	70.0	5.0	60
The frequency of VAT tax returns and listings	35.0	55.0	10.0	60
The complexity of VAT tax returns and listings	16.7	73.3	10.0	60
Invoicing requirements	20.0	73.3	6.7	60
Repayment and refund requirements	8.3	76.7	15.0	60
Accessing tax information and contacting tax officials	18.3	68.3	13.3	60
Record keeping requirements	25.0	65.0	10.0	60
Audits and litigation	8.3	61.7	30.0	60
Weighted %	Not a difficulty	A difficulty	Don't know/Missing	Responses
Identification and registration	25.3	68.7	5.9	57
The frequency of VAT tax returns and listings	27.0	61.4	11.6	57
The complexity of VAT tax returns and listings	18.2	70.1	11.6	57
Invoicing requirements	21.2	70.6	8.2	57
Repayment and refund requirements	7.1	77.2	15.7	57
Accessing tax information and contacting tax officials	26.1	63.7	10.2	57
Record keeping requirements	20.8	69.7	9.5	57
Audits and litigation	7.5	65.8	26.7	57

Note: Percentages in bold are different from zero at a 5% level of significance (see Annex D).

The weighted figures in Table 3-9 indicate that a majority of large companies registered in another EU Member State without having a permanent establishment there have difficulties with regard to all VAT obligations. The most problematic issues are the repayment and refund requirements (77.2% having difficulties), invoicing requirements (70.6%) and the complexity of tax returns and listings (70.1%).

These results can be compared with the estimates obtained from the same sample of 60 large companies concerning domestic VAT obligations (see Table 3-10).

Table 3-10 Comparison of opinions for large companies registered in a Member State where they don't have a permanent establishment

% indicating a difficulty (weighted results)	Domestic VAT obligations	VAT obligations in other MS	Comparison (+ indicate more difficulty abroad)
Identification and registration	37.1	68.7	+++
The frequency of VAT tax returns and listings	44.0	61.4	++
The complexity of VAT tax returns and listings	64.0	70.1	+
Invoicing requirements	69.3	70.6	+
Repayment and refund requirements	53.4	77.2	++
Accessing tax information and contacting tax officials	46.4	63.7	++
Record keeping requirements	74.4	69.7	—
Audits and litigation	86.0	65.8	---

Note: Percentages in bold are different from zero at a 5% level of significance (see Annex D).

This table highlights that for large companies, VAT obligations abroad are most of the time felt to lead to more difficulties than domestic VAT obligations. Differences of opinion are particularly striking when it comes to identification and registration (68.7% vs. 37.1%), repayment and refund requirements (77.2% vs. 53.4%) and accessing tax information and contacting tax officials (63.7% vs. 46.4%). However, it should also be noted that the results also indicate that regarding record keeping requirements and audits and litigation, difficulties in the domestic context are felt to be higher than with regard to obligations in other EU countries, because in these cases there is no obligation to keep records abroad and the chance to be audited is less important. The outcome is in general not surprising, because foreign law, administration, language, etc. is not as well known as domestic and it is difficult to deal with all foreign obligations without having any contact person in the Member States. For example, getting a VAT number registration means that companies have to contact a foreign administration and fill in a form in a foreign language. This explains why the Commission is suggesting introducing a one-stop-shop mechanism for these companies, which would enable them to comply with all their obligations in their country of establishment (see Box 3-7 below).

Some of these results, in particular with regard to repayment and refund requirements, can usefully be compared with more specific results obtained in the regression analysis presented in Chapter 2. It should be underlined that no evidence was found of higher VAT compliance costs for companies that are registered in an EU Member State without having a permanent establishment there and which did not incur VAT on inputs abroad. However, companies which are registered in another EU Member State without a permanent establishment there and which incurred a VAT on inputs abroad were associated with significantly higher VAT compliance costs. This highlights the impact of VAT on inputs incurred abroad and the problem of repayment and refund requirements.

Box 3-7 VAT One-Stop-Shop

The Commission intends to make a proposal in the autumn of this year on a VAT One-Stop-Shop. This special scheme would be an optional and fully electronic compliance scheme that would be open to every trader supplying goods or services that are subject to VAT to customers in Member States other than that in which he is established.

The scope of the scheme would be limited to supplies made by business to consumers (B2C). The simplest way of reducing onerous compliance obligations for business-to-business (B2B) supplies would be to change the VAT rules so that the customer (if he is a trader) rather than the supplier would be responsible for paying the VAT on services supplied to him.

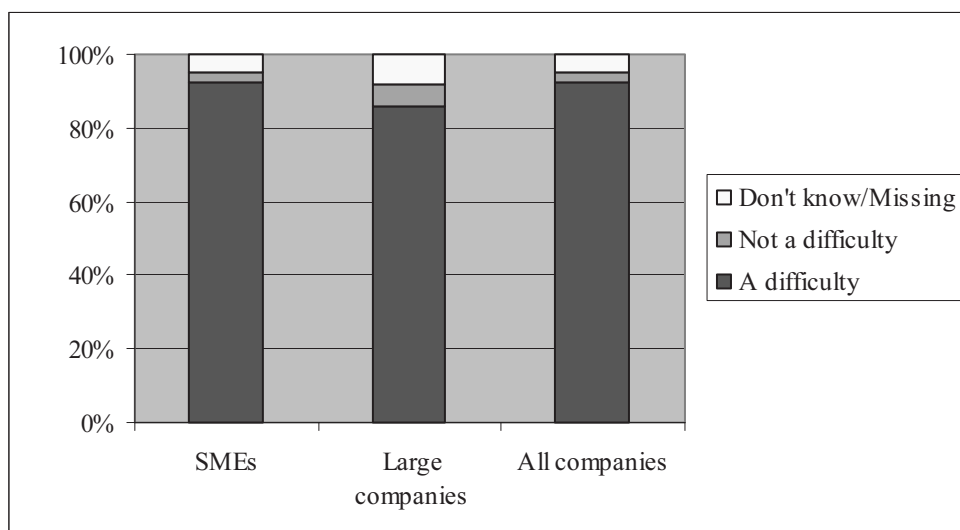
The scheme would allow a trader to register only once in the Member State where he is established and to use a single VAT number for all B2C supplies made within the scope of the scheme. VAT declarations would be made to one single electronic portal and would then be submitted automatically to the different Member States to which the trader supplies goods or services. Payments would be made directly to the Member State of consumption, possibly with the help of financial intermediaries.

A consultation of businesses on the One-Stop-Shop was closed on 31 July 2004 (see http://europa.eu.int/comm/taxation_customs/taxation/consultations/one_stop_en.htm)

3.3.4. Opinions on the 8th VAT Directive

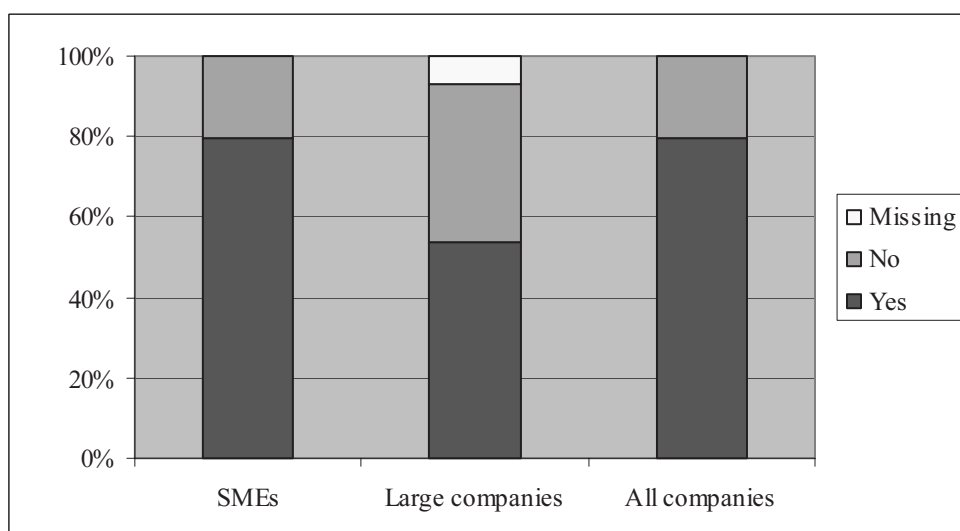
The analysis above, and in particular the regression analysis presented in section 2-6 of chapter 2, highlights that repayment and refunds requirements are a particular concern to many large companies and lead to higher compliance costs. This does not come as a surprise as companies often complain about this issue. Therefore, this issue has been examined more closely in the European Tax Survey and more specific questions asked in this respect. Of the 700 companies, 200 responded to be subject to VAT in another EU Member State in which they are not registered. For those companies two questions on refunding through the 8th Directive have been asked. The results are presented in Graphs 3-14 and 3-15 below.

Graph 3-14 Opinions on refunds through the 8th Directive procedure (weighted results)



Graph 3-15 Information on not requested refunding (weighted results)

Question: Have you ever not requested refunding because of the complexity or length of procedures?



These Graphs 3-14 and 3-15 convey two main messages. First, the weighted estimates indicate that 92.3% of SMEs and 86.1% of large companies incurring VAT costs on their inputs in an EU Member State without being registered have difficulties coping with procedures for refunds under the 8th Directive. Second, an estimated 79.7% of SMEs and 53.5% of large companies have not requested refunding at some point because of the complexity or the length of the procedure. These figures are quite significant and seem to confirm the existence of substantial problems resulting from the procedure for refunds under the 8th directive (see Box 3-8). As indicated in Box 3-8, despite lengthy efforts to simplify refunds procedures, it has not been possible yet to achieve the necessary progress in that area.

Box 3-8 The 8th Directive procedure

The 8th Directive procedure is a very heavy and complex procedure for traders. This was already identified as a major hinder to the smooth functioning of the Internal Market at the time of the SLIM initiative. SLIM stands for **Simpler Legislation for the Internal Market** and was launched by the Commission in May 1996. It was targeted at identifying ways in which existing internal market legislation (not only taxation but in general) could be simplified.

As a result, the Commission proposed in 1998 to replace the 8th Directive procedure by a right of refund in the country of establishment (with an appropriate clearing system between Member States). Due to a lack of political will from several Member States in order to move towards such a system the discussions are currently stalled in the Council.

In the near future, the Commission may propose an electronic system of reimbursement for those refunds, on the model of the proposed VAT One-Stop-Shop.

3.4. Taxation and cross-border activities in the European Union

It is often argued that tax obligations may have an impact on cross-border activity, in particular investment decisions and decisions related to companies structures. In other words, the functioning of the single market may be affected by taxation. Therefore, a part of the questionnaire submitted to companies participating in the European Business Test Panel concerned the influence of taxation on investment and other business decisions.

In what follows, questions relate first to decisions to abstain from performing VAT activities because of compliance requirements. In a way, this question bears on "non-activities" in the EU because of taxation, an issue which is rarely examined. Next, companies were asked to indicate whether taxation could influence the choice of location of specific activities and, more generally, how important taxation is in deciding on investments in the EU. Lastly, attention was given to the impact of taxation on the structure of financing of companies involved in foreign operations.

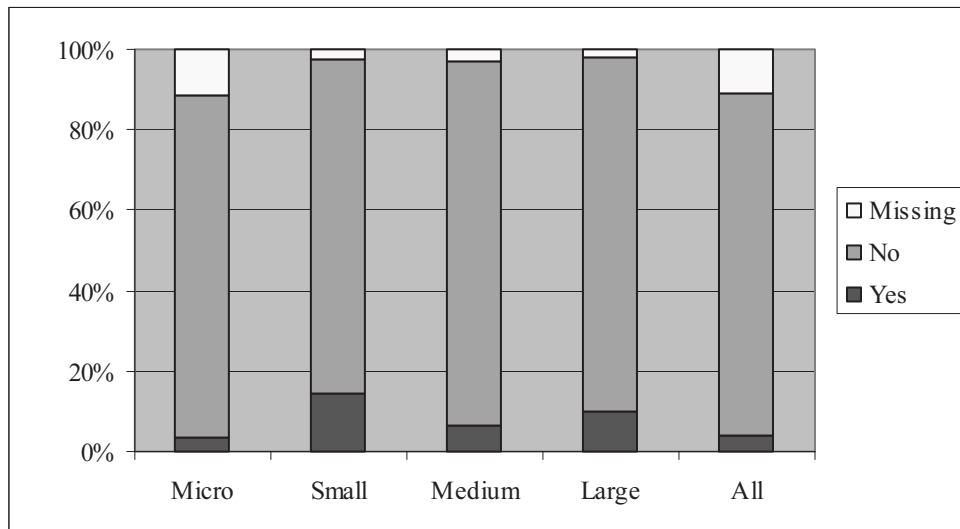
3.4.1. Launching VAT taxable activities in other Member States

The purpose of the following question is to identify whether the existence of VAT obligations has an impact on company decisions to carry out cross-border VAT taxable activities. The following question was asked to the 603 respondents which reported not to carry out VAT activities in another EU member state (where they do not have a permanent establishment).

Question:

"Are VAT compliance requirements the reason why your firm has not carried out VAT taxable activities in another Member State (where it does not have a permanent establishment)?"

Graph 3-16 Opinions on impact of VAT compliance requirements on VAT taxable activities in another Member State (weighted results)



The weighted results highlight in particular that 14.2% of small companies and 9.9% of large companies have not carried out VAT taxable activities in another Member State (where they do not have a permanent establishment) because of VAT compliance requirements. Figures for micro and medium companies are lower (3.5% and 6.4% respectively).

One should be cautious when interpreting these results based on the responses obtained in the European Tax Survey. First, the figures do not give information of the extent of activities that were not implemented as a result of VAT requirements. They just indicate that, for a small percentage of companies, a decision has been taken at some point not to undertake a specific cross-border VAT taxable activity because of VAT requirements. One may reasonably assume that the types of activities foregone were marginal for the companies. Otherwise, it would probably have incurred the necessary costs. Nevertheless, the result obtained here constitutes an interesting indication that compliance requirements linked to VAT do have an effect at the margin on cross-border activities in the Internal market, which could in turn have a negative impact on the process of European economic integration. The implementation of a one-stop-shop mechanism (see Box 3-7) could reduce the number of companies which are not active abroad due to VAT compliance requirements.

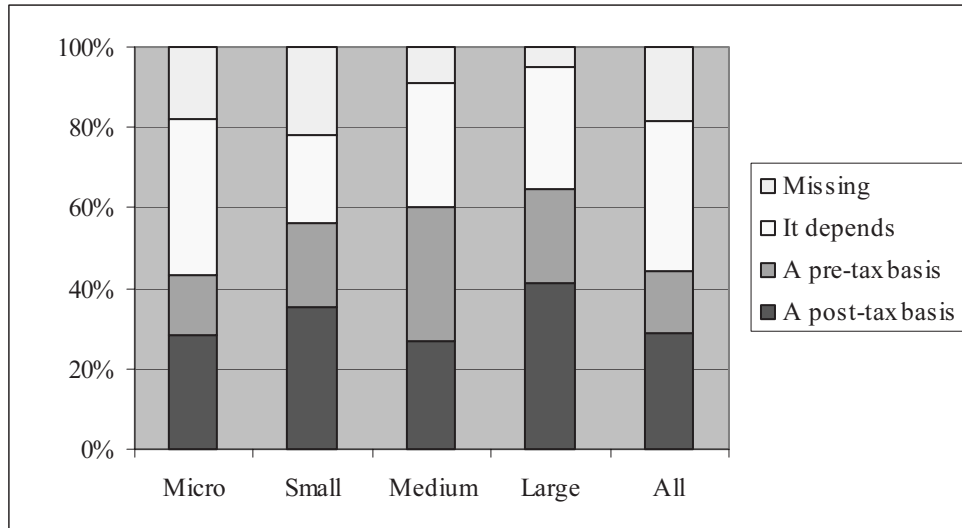
3.4.2. *Investing in other Member States*

Taxation may affect the form and the location of investments. This has notably been highlighted in a survey carried out for the Ruding Report (1991). In order to have a better insight on this issue, a number of questions were asked to the participants to the European Tax Survey regarding the link between taxation and investment. The first question focused on decisions to invest. Do companies actually assess investments with regard to tax circumstances? Following that, special attention was placed on identifying the type of activities for which the location is more likely to be influenced by taxation concerns.

Question:

"When taking investment decisions, does your firm produce investment appraisal calculations on ..."

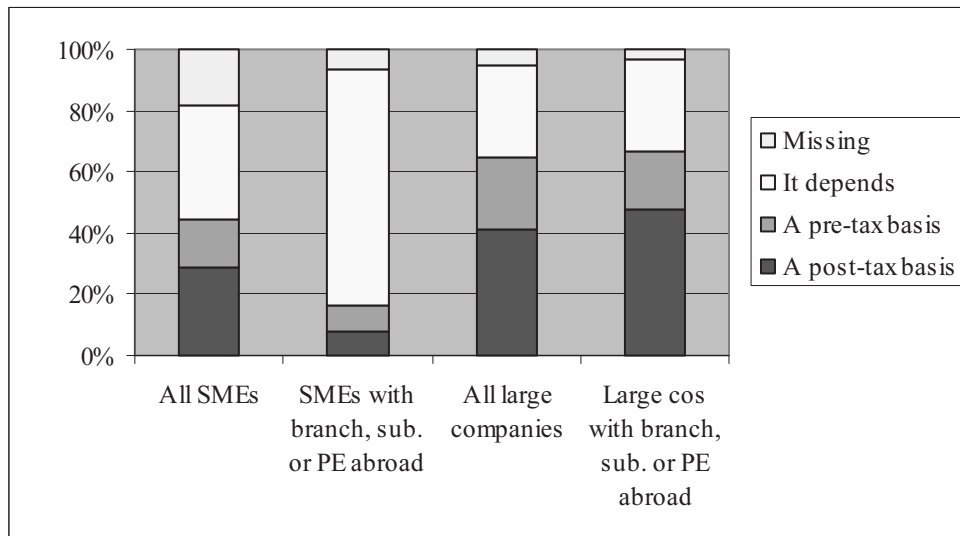
Graph 3-17 Information on investment appraisal calculations



The weighted results indicate that 28.7% of businesses evaluate their investment opportunities on a post-tax basis, while 15.6% of companies evaluate their investments on a pre-tax basis. At the same time, 37.5% of companies of all size evaluate their investments either on a post-tax basis or on a pre-tax basis depending on the type of investment to carry out.

In the context of a survey that is primarily focused on cross-border activities, it is interesting to compare these results with results obtained for firms having a branch, a subsidiary or a permanent establishment (PE) in another Member State. This comparison is done for SMEs and large companies (165 companies).

Graph 3-18 Practices related to investment appraisal (SMEs vs. large companies)



Graph 3-18 above shows that 48.0% of the large companies with a branch, a subsidiary or a permanent establishment in another Member State assess their investments on a post-tax basis. This figure is higher than the one obtained for the whole population, including these large companies. This suggests that large companies with cross-border activities pay significantly more attention to tax issues when deciding on their investments than the others do. The responses for SMEs having a branch, a subsidiary or a permanent establishment abroad differ from the responses obtained for all SMEs. The main difference relates to the fact that 72% of the companies indicated that the type of appraisal "depends" on the circumstances. Although one cannot infer directly from this result that SMEs with cross-border activities are more prone to establish post-tax appraisals for their investments, this result nevertheless suggests that cross-border activities require a cautious evaluation of tax aspects in some cases. At the same time, due to a low number of responses, results on SMEs with a branch, a subsidiary or a permanent establishment abroad are potentially not very reliable.

The following question relating to investment bears on cross-border investment location. The results presented here focus on companies having a subsidiary, a branch or a permanent establishment in another EU country than their home country.

Question:

"Respondents have been asked to indicate for each of the following factors whether taxation influences their choice of location."

The weighted results presented in Table 3-13 indicate that more than 50% of large companies with a subsidiary, a branch or a Permanent establishment in another Member State are influenced by taxation in their choice of location for production plants, sales outlets, coordination centers and financial services centers. On the other hand, only 34.4% are influenced by taxation for locating their research and development centers.

Table 3-11 Influence of taxes on location and investments

Un-weighted %	SMEs				Large companies			
	Never	Sometimes always	Don't know/ Missing	Responses	Never	Sometimes always	Don't know/ Missing	Responses
Production plant	26.9	38.5	34.6	52	13.3	54.0	32.7	113
Sales outlet	18.9	26.7	54.4	52	23.9	40.4	35.7	113
Coordination centre	23.1	21.2	55.8	52	12.4	50.4	37.2	113
Financial services centre	23.1	21.2	55.8	52	9.7	48.7	41.6	113
Research and development centre	13.5	30.8	55.8	52	15.9	38.9	45.1	113

Weighted %	SMEs				Large companies			
	Never	Sometimes always	Don't know/ Missing	Responses	Never	Sometimes always	Don't know/ Missing	Responses
Production plant	7.4	14.5	78.0	51	11.1	57.7	31.2	113
Sales outlet	12.5	13.8	73.7	51	28.2	50.6	21.2	113
Coordination centre	6.2	3.7	90.1	51	9.0	57.0	33.9	113
Financial services centre	4.0	7.4	88.6	51	5.2	51.2	43.5	113
Research and development centre	2.2	10.6	87.2	51	19.4	34.4	46.3	113

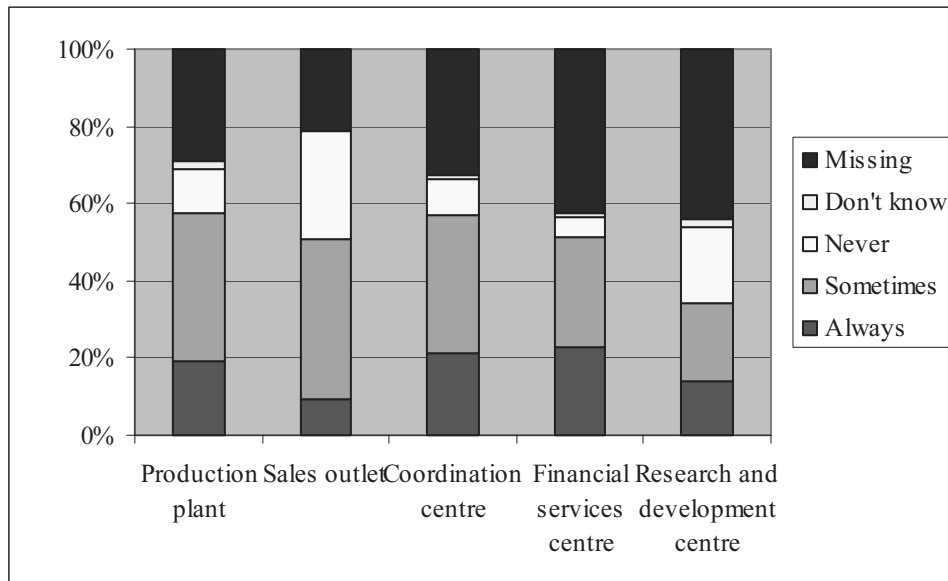
Note: Percentages in bold are different from zero at a 5% level of significance (see Annex D).

However, a significant percentage of companies did not provide a response to that question. This may refer to the fact that some of the structures being scrutinized, such as coordination centers, financial services centers and R&D centers are only used by a few companies, for which tax circumstances do affect the choice of location. This interpretation is reinforced by the fact that only a small percentage of firms indicate "never" being influenced by taxation when deciding on the choice of location for coordination centers or financial services centers and that few companies actually responded "don't know" to the question (see Graph 3-19 below).

Overall, these results suggest that taxation could influence the location of specific operations of companies, such as production plants, coordination centers or financial services centers. However, only a part of companies having cross-border activities appear to set up such kind of operations. At the same time, the location of sales

outlets seems less influenced by tax factors. This reflects the fact that the location of the market, i.e. the customers, has a bigger influence on the location of sales outlets than other factors. Last, the location of research and development centers seem only relatively sensitive to tax incentives. This is surprising, as several states have set up tax incentives to attract foreign R&D activities (or keep their domestic activities in that area). One hypothesis is that Member States' tax incentives counterbalance one another in the location decision of research centers.

Graph 3-19 Influence of taxes on location of investments (large firms, weighted results)



It is interesting to note that broadly similar conclusions were obtained in the context of the Ruding survey, which examined the influence of taxation on decisions regarding the location of international operations. In its analysis of the results of the survey, Devereux (1992) notes that "the location of a sales outlet must be heavily dependent on the location of the market in which the goods are to be sold – hence taxation is less important than the location of the market. By contrast, the location of a financial service center is much less important, given modern communications". Considering applicable responses only, the Ruding survey highlighted that production plants, financial service centers and coordination centres were the activities where taxation was most likely to be always a relevant consideration and a major factor in the location decision. This result is similar to the one found in this European Tax Survey.

3.4.3. *Merging or acquiring another business in the EU*

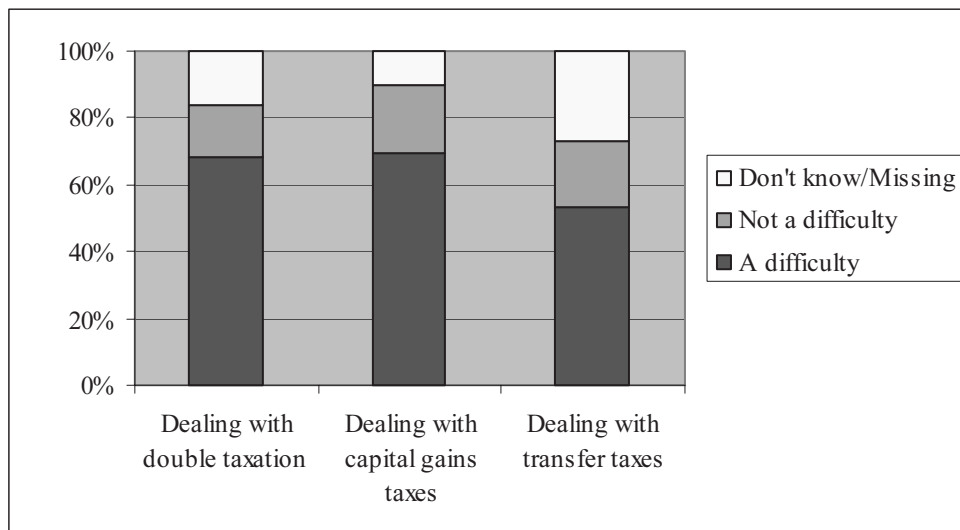
Cross-border investments in the European Union often occur through mergers and acquisitions of foreign firms. Furthermore, the European Community has been active in that area, notably through the Council Directive on mergers and acquisitions. Specific questions were therefore asked to companies on this topic, which was also identified as one problematic issue in Section 3.2 above.

Out of the 700 respondents, 145 reported to have merged with or acquired another business in the EU during the past 5 years. For those 145 respondents three questions related to mergers and acquisitions were asked. Results are presented only for the 90 large companies.

Question:

"Mergers and acquisitions can pose problems. Some of these are listed below. Please give your opinion on each of them."

Graph 3-20 Opinions on specific issues linked to mergers and acquisitions (large firms, weighted results)



The weighted results presented in Graph 3-20 indicate that a majority of companies which merged with- or acquired another business in the EU during the past 5 years encountered difficulties. In particular, 69.4% of companies had difficulties regarding capital gain taxes, while dealing with double taxation is reported as a difficulty for 68.1% of the companies. Dealing with transfer taxes is a difficulty to 53.4% of companies.

The question arises as to how to interpret the results. Do difficulties mean a dissatisfaction with regard to taxes paid? Or do respondents have more fundamental problems in these areas? Whereas, the analysis does not provide a clear answer to these questions, it has the merit of highlighting the fact that most companies dealing with cross-border mergers or acquisitions do consider dealing with double taxation, capital gains taxes and, to a lesser extent, transfer taxes a problem.

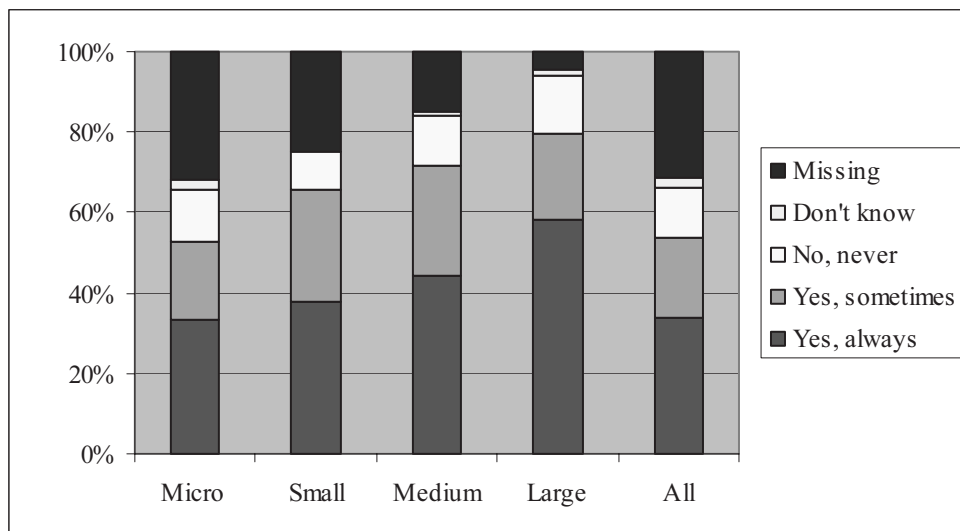
3.4.4. *Company structure and taxes*

Taxation can influence company structures and financing. In what follows, two questions are asked. The first examines the importance of the tax department in the decision-taking process of a company. The next question scrutinizes the impact of taxation on specific issues relating to the structure and the financing of companies.

Question:

"When taking internal management decisions concerning the corporate structure of your firm, such as establishing new subsidiaries, branches or permanent establishments, is approval from your tax department or tax advisors required?"

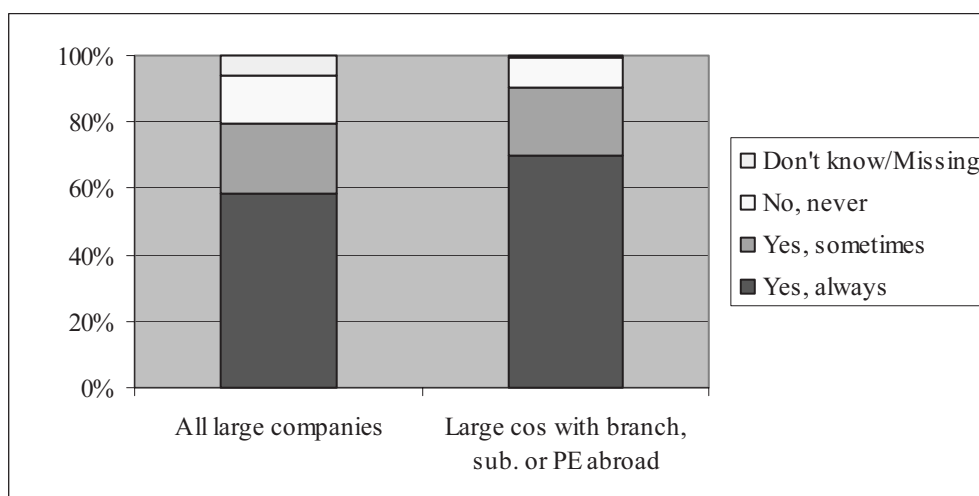
Graph 3-21 Management decisions concerning corporate structure (weighted results)



The weighted figures indicate that 33.7% of all companies always require the approval of their tax department or tax advisors when taking some decisions as to the corporate structure of the company. In addition, 20.1% of all companies sometimes require such an approval. Responses vary according to the size of companies. In particular, percentages related to the systematic approval of the tax department or tax advisors increases with the size of companies (from 33.3% for micro companies to 58.5% for large companies). Overall, the implication of the tax department in decisions on corporate structures appears more marked for large companies than for SMEs.

In order to have better information concerning firms active in several EU Member States, the above results have been compared with results obtained for firms having a branch, a subsidiary or a permanent establishment in another Member State. This comparison is done for large companies, for which there was a sufficient number of responses (113).

Graph 3-22 Comparison of results for large companies (weighted results)



Graph 3-22 shows that when taking internal management decisions concerning the corporate structure of the firm, such as establishing new subsidiaries, branches or permanent establishments, the approval from the tax department or tax advisors is required "sometimes" or "always" in 90.1% of the large companies with a branch, a subsidiary or a permanent establishment in another Member State. This figure is higher than the one obtained for all large companies (79.5%), including the ones with a branch, a subsidiary or a permanent establishment in another Member State. This suggests that large companies with cross-border activities pay significantly more attention to tax issues when deciding on their structure than the others do.

The results above present a general view, encompassing all kinds of possible situations. What follows (see Table 3-12) focuses on specific decisions relating to the structure of the firms and their financing.

Question:

"Taxes can be a factor when it comes to deciding on the financial and legal structure of your international operations. Different ways of structuring international operations are indicated below. Please indicate, for each of them, if taxes are a factor."

The weighted results highlight the importance of tax considerations as a factor when it comes to deciding on the financial and legal structure of the international operations of large EU firms. More than 60% of large firms having a branch, a subsidiary or a permanent establishment in another EU Member State considered that taxes is a factor for all the issues examined. Particularly striking is the fact that 87.3% of the companies are influenced by taxes for deciding whether foreign operations should be organised through a subsidiary, a branch or a permanent establishment. 77.2% of the companies consider tax as a factor when they decide to use new equity or debt when financing foreign operations directly or indirectly via the parent company. Slightly lower figures can be observed with regard to decisions as to the local financing offoreign operations. These figures can usefully be compared with those obtained in the Ruding survey (see Box 3-9).

Table 3-12 Impact of taxation on the financial and legal structure of international operations

Un-weighted % (large firms with a subsidiary, a branch or a PE in another MS)	Never	Sometimes/ always	Don't know/Missing	Responses
Organisation foreign operations through a subsidiary, branch or permanent establishment	7.1	85.0	8.0	113
Financing foreign operations locally, rather than directly or indirectly via the parent company	12.4	75.2	12.4	113
Use new equity or debt when financing foreign operations directly or indirectly via the parent company	8.9	77.9	13.3	113
Route income flowing to or from foreign operations through holding companies or through intermediaries in a third country	17.7	59.3	23.0	113
Use local borrowing, local equity issues or retained earnings, when financing foreign operations locally	8.0	74.3	17.7	113
Weighted % (large firms with a subsidiary, a branch or a PE in another MS)	Never	Sometimes/ always	Don't know/Missing	Responses
Organisation foreign operations through a subsidiary, branch or permanent establishment	4.8	87.3	7.9	113
Financing foreign operations locally, rather than directly or indirectly via the parent company	14.1	74.9	11.0	113
Use new equity or debt when financing foreign operations directly or indirectly via the parent company	12.5	77.2	10.3	113
Route income flowing to or from foreign operations through holding companies or through intermediaries in a third country	13.5	60.9	25.7	113
Use local borrowing, local equity issues or retained earnings, when financing foreign operations locally	11.3	70.0	18.7	113

Note: Percentages in bold are different from zero at a 5% level of significance (see Annex D).

Box 3-9 Comparison with the Ruding survey

A comparison of these results with the results obtained in the context of the Ruding survey, which asked almost identical questions, shows interesting similarities. In its presentation of the results, Devereux (1992) indicates that "the overwhelming impression" is that tax is "extremely important" in decisions regarding the financial and legal structure of companies' international operations. "The decisions as to 'whether to organise foreign operations through a subsidiary or a branch' and how to finance the operation, whether locally or directly from the parent or whether to use equity or debt all received responses indicating that around eighty per cent or respondents considered taxation to be (...) always or usually a major factor. Slightly lower responses (...) were found for the last decision 'whether or not to route income flowing to or from foreign operations through holding companies or other intermediaries in a third country other than that where the parent or foreign operation is located. Clearly, these responses confirm that taxation is an important factor in the financing and structuring of foreign operations'".

It should be noted that the figures presented by Devereux cover only applicable responses, i.e. 'don't know' or missing answers were not taken into account in percentages.

3.5. Conclusion

The analysis of companies' opinion on a number of issues related to company taxation and VAT led to a number of interesting results.

Company taxation

The responses provided by companies participating in the European Tax Survey highlight that tax accounting and record keeping requirements and audits and litigations are the issues related to company taxation which raise the main concerns in the domestic context.

In relation to foreign-sourced income, the results highlight that companies with a branch, a subsidiary or a permanent establishment in another EU Member State have particular difficulties with regard to audits and litigations (large companies) and acquiring information and contacting tax administrations.

With regard to specific issues that could constitute tax obstacles to the proper functioning of the Internal market, the estimates indicate that transfer pricing is an important issue for more than eighty percent of SMEs and large companies. In particular, with regard to transfer pricing, dealing with documentation requirements is considered as a difficulty for 81.9% of large companies. It should be noted that in the Ruding report (1991) transfer pricing was considered as a relatively minor issue.

VAT

Four issues raise particular difficulties for companies involved in the European Tax Survey in the domestic context, namely audits and litigations, record keeping requirements, the complexity of tax returns and listings and invoicing requirements.

In relation to VAT obligations in other Member States, one issue appears particularly problematic for large companies³⁰, namely the repayment and refund requirements. Other issues, such as accessing tax information and contacting tax officials and audits and litigations also appear to lead to difficulties. Whereas the first issue is specific to VAT, it should be noted that the other issues also appear as particular difficulties concerning company taxation.

The opinions on the same issues related to VAT by companies registered in a Member State where they do not have a permanent establishment shows that repayment and refunds requirements are the first issue of concern. In fact, 86.1% of large companies incurring VAT costs on their inputs in an EU Member State without being registered are estimated to have difficulties coping with procedures for refunds under the 8th VAT directive. The complexity or the length of the procedures are such that an estimated 53.5% of large companies have not requested refunding at some point. These are obviously striking results, which also confirm the widespread criticism on the current procedures and the difficulties they imply.

Other taxation issues in the Internal market

Based on the responses obtained in the European Tax Survey, the results highlight that 14.2% of small and 9.9% of large companies have not carried out VAT taxable activities in another Member State where they do not have a permanent establishment because of VAT compliance requirements. One may assume that the types of activities that were not undertaken were not principal to the businesses in question or really profitable (otherwise one may reasonably assume that the necessary costs would have been incurred). Nevertheless, this result suggests that, at the margin, VAT requirements may make it particularly difficult for companies to start activities in another Member State in which they don't have a regular business. In the long run, this may be damaging for the Internal market as less cross-border activities are undertaken, and hence less investments and possibly lower economic growth.

Taxation also influences investments in the Internal market. The results highlight that taxation is a relevant factor mainly for the location of production plants, coordination centres and financial services centres. When it comes to mergers and acquisitions, taxation could also prove a serious issue. In fact, 69.4% of companies which merged with- or acquired another business in the EU during the past five years indicated having difficulties regarding capital gain taxes. 68.1% reported difficulties linked to double taxation. These results suggest that capital export neutrality, i.e. the identical taxation of investment whatever its destination, is not respected everywhere in the EU and that taxation could distort the choice of location, thereby decreasing the efficiency of investment. In addition, the incompatibility of Member States' tax systems may lead to problems of double taxation or increased taxation in cases of mergers and acquisitions. This can have a negative impact on that kind of undertakings.

Furthermore, the analysis shows that tax conditions affect companies' decisions concerning the financial and legal structure of their international operations.

³⁰ It was not possible to provide meaningful results for SMEs due to the small number of responses for SMEs.

Particularly striking is the fact that 87.3% of the large companies with a subsidiary, a branch or a permanent establishment abroad indicate that taxes can influence decisions on whether foreign operations should be organised through a subsidiary, a branch or a permanent establishment. An estimated 77.2% of these large companies consider tax as a factor when they decide to use new equity or debt when financing foreign operations directly or indirectly via the parent company. It should be noted that comparisons with responses provided by companies active only in the domestic context highlights that companies with cross-border activities are significantly more sensitive to taxation when deciding the financial and legal structure of their operations.

4. CONCLUSIONS

Four main conclusions can be drawn from the European Tax Survey.

First, beyond the usual caveats linked to the treatment of estimates provided in surveys and the specific limitations linked to the low number of responses in the European Tax Survey (see Section 1.3), one can say that compliance costs linked to VAT and company taxation are significant and they can impose a substantial burden of companies, in particular SMEs. Compliance costs related to company taxation appear to be higher than compliance costs related to VAT.

Second, the existence of different tax systems in the EU, both for VAT and company taxation, impose larger costs on companies having cross-border activities. Higher compliance costs can in particular be observed for companies having VAT activities in other Member States without having a permanent establishment or for companies that underwent transfer pricing controls.

Third, some issues seem to impose a significant burden to companies and could affect their cross-border activities in the EU. An issue of common concern is the difficulty linked to finding information on foreign tax systems and contacting foreign tax officials. In addition some specific issues raise additional problems. For example, the case of transfer pricing (documentation) requirements and the difficulties linked to the refunds under the 8th VAT directive and activities abroad without a permanent establishment.

Fourth, taxation affects many decisions of companies regarding their international operations. Decisions concerning the legal structure and the financing of companies are often affected by taxation. So is the location of some of their investments. In addition, VAT requirements may lead to not undertaking some cross-border VAT taxable activities, while tax rules may lead to double or higher taxation in cases of mergers and acquisitions.

These results suggest that the current organisation of taxation in the EU leads to numerous economic distortions and affects the proper functioning of the Internal market. Further research should be conducted with a larger number of companies, more representative of the EU, in order to provide specific country and sector results, and facilitate comparisons between responses provided by companies of varying sizes.

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ANNEXES

ANNEX A - QUESTIONNAIRE

Structure Questionnaire

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	The questions 23-39 are only asked to companies that responded "Yes" to Question 22	
III-3.1	Company Taxation - Income in other EU Member States	Questions 23-26
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	Questions 41-43 are only asked to companies that responded "Yes" to Question 40	
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	The questions 49-57 are only asked to companies that responded "Yes" to Question 48	
	Question 58 is only asked to companies that responded "No" to Question 48	
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0. Identification of case for EBTP

Question 1 Indicate your main sector of activity:

- ☐ D - Manufacturing
- ☐ J - Financial intermediation
- ☐ G - Wholesale and retail trade
- ☐ F - Construction
- ☐ I - Transport, storage and communication
- ☐ K - Real estate, renting and business activities
- ☐ O - Other community, social and personal service activities
- ☐ H - Hotels, restaurants and bars
- ☐ N - Health and social work
- ☐ E - Electricity, gas and water supply
- ☐ C - Mining/Quarrying

Question 2 Indicate in which EU/EEA countries your company is based?

- ☐ DA - Denmark
- ☐ NL - The Netherlands
- ☐ UK - United Kingdom
- ☐ DE - Germany
- ☐ IT - Italy
- ☐ PT - Portugal
- ☐ FI - Finland
- ☐ AT - Austria
- ☐ SV - Sweden
- ☐ IE - Ireland
- ☐ NO - Norway
- ☐ BE - Belgium
- ☐ ES - Spain
- ☐ IS - Island
- ☐ FR – France
- ☐ EL - Greece

☐ LU - Luxembourg

Question 3 Number of employees in your company

☐ 0

☐ 1-9

☐ 10-49

☐ 50-249

☐ 250-499

☐ 500 +

Question 4 Apart from your country, in how many countries of the European Union do you regularly sell products and services?

☐ none

☐ 1

☐ 2-3

☐ 4-5

☐ more than 5

I. Financial Year

Question 5 For which accounting year do your answers refer to? Please use data for the most recent complete financial year. Year ended...:

☐ September 2002

☐ October 2002

☐ November 2002

☐ December 2002

☐ January 2003

☐ February 2003

☐ March 2003

☐ April 2003

☐ May 2003

☐ June 2003

☐ July 2003

☐ August 2003

☐ September 2003

II. Company Information

Question 6 Your company is ...

- ☐ an independent company
- ☐ a subsidiary/a member of a group
- ☐ the parent company of a group

Question 7 How many subsidiaries, branches or permanent establishments does your firm have in your home Member State?

- ☐ none
- ☐ 1-5
- ☐ 6-15
- ☐ 16-50
- ☐ more than 50

Question 8 How many subsidiaries, branches or permanent establishments does your firm have in other EU Member States?

- ☐ none
- ☐ 1-5
- ☐ 6-15
- ☐ 16-50
- ☐ more than 50

Question 9 In which part of the world is the ultimate parent company of your group based?

- ☐ in the European Union
- ☐ outside the European Union

III-1 Company Taxation - Domestic Income

Question 10 Tax accounting/record keeping is:

- ☐ not a difficulty
- ☐ a moderate difficulty
- ☐ an important difficulty
- ☐ do not know
- ☐ not applicable

Question 11 Acquiring information on tax laws and regulations is:

- ☐ not a difficulty

- ☐ a moderate difficulty
- ☐ an important difficulty
- ☐ do not know
- ☐ not applicable

Question 12 Contacting tax administrations or tax officials is:

- ☐ not a difficulty
- ☐ a moderate difficulty
- ☐ an important difficulty
- ☐ do not know
- ☐ not applicable

Question 13 Audits and litigation are:

- ☐ not a difficulty
- ☐ a moderate difficulty
- ☐ an important difficulty
- ☐ do not know
- ☐ not applicable

III-2 VAT - Domestic Activities

Question 14 Identification and registration is:

- ☐ not a difficulty
- ☐ a moderate difficulty
- ☐ an important difficulty
- ☐ do not know
- ☐ not applicable

Question 15 The frequency of VAT tax returns and listings is:

- ☐ not a difficulty
- ☐ a moderate difficulty
- ☐ an important difficulty
- ☐ do not know
- ☐ not applicable

Question 16 The complexity of VAT tax returns and listings is:

- ☐ not a difficulty
- ☐ a moderate difficulty
- ☐ an important difficulty
- ☐ do not know
- ☐ not applicable

Question 17 Invoicing requirements are:

- ☐ not a difficulty
- ☐ a moderate difficulty
- ☐ an important difficulty
- ☐ do not know
- ☐ not applicable

Question 18 Repayment and refund requirements are:

- ☐ not a difficulty
- ☐ a moderate difficulty
- ☐ an important difficulty
- ☐ do not know
- ☐ not applicable

Question 19 Accessing tax information and contacting tax officials are:

- ☐ not a difficulty
- ☐ a moderate difficulty
- ☐ an important difficulty
- ☐ do not know
- ☐ not applicable

Question 20 Record keeping requirements are:

- ☐ not a difficulty
- ☐ a moderate difficulty
- ☐ an important difficulty
- ☐ do not know
- ☐ not applicable

Question 21 Audits and litigation are:

- ☐ not a difficulty
- ☐ a moderate difficulty
- ☐ an important difficulty
- ☐ do not know
- ☐ not applicable

III-3 Subsidiary/Branches/Permanent Establishments - Company Taxation and VAT

Question 22 Does your firm have a subsidiary, branch or permanent establishment in another EU Member State?

- ☐ No
- ☐ Yes

Questions 23-39 are only asked to companies that responded "Yes" to Question 22.

III-3.1 Company Taxation – Income in other EU Member States

Question 23 Tax accounting/record keeping is:

- ☐ not a difficulty
- ☐ a moderate difficulty
- ☐ an important difficulty
- ☐ do not know
- ☐ not applicable

Question 24 Acquiring information on tax laws and regulations is:

- ☐ not a difficulty
- ☐ a moderate difficulty
- ☐ an important difficulty
- ☐ do not know
- ☐ not applicable

Question 25 Contacts with tax administrations or tax officials are:

- ☐ not a difficulty
- ☐ a moderate difficulty
- ☐ an important difficulty
- ☐ do not know

☐ not applicable

Question 26 Audits and litigation are:

☐ not a difficulty

☐ a moderate difficulty

☐ an important difficulty

☐ do not know

☐ not applicable

☐ do not know

III-3.2 Company Taxation - Obstacles to cross-border activity

Question 27 The absence of cross-border loss compensation:

☐ not important

☐ quite important

☐ very important

☐ not applicable

☐ do not know

Question 28 Double taxation on repatriated profits and other income from subsidiaries and branches (e.g. dividends, interest, royalties):

☐ not important

☐ quite important

☐ very important

☐ not applicable

☐ do not know

Question 29 Transfer pricing:

☐ not important

☐ quite important

☐ very important

☐ not applicable

☐ do not know

Question 30 Taxation of mergers and acquisitions:

☐ not important

☐ quite important

- ☐ very important
- ☐ not applicable
- ☐ do not know

Question 31 Costs of dealing with different national tax systems:

- ☐ not important
- ☐ quite important
- ☐ very important
- ☐ not applicable
- ☐ do not know

III-3.3 VAT - Activities in other EU Member States

Question 32 Identification and registration is:

- ☐ not a difficulty
- ☐ a moderate difficulty
- ☐ an important difficulty
- ☐ do not know
- ☐ not applicable

Question 33 The frequency of VAT tax returns and listings is:

- ☐ not a difficulty
- ☐ a moderate difficulty
- ☐ an important difficulty
- ☐ do not know
- ☐ not applicable

Question 34 The complexity in VAT tax returns and listings is:

- ☐ not a difficulty
- ☐ a moderate difficulty
- ☐ an important difficulty
- ☐ do not know
- ☐ not applicable

Question 35 Invoicing requirements are:

- ☐ not a difficulty

- ☐ a moderate difficulty
- ☐ an important difficulty
- ☐ do not know
- ☐ not applicable

Question 36 Repayment and refund requirements are:

- ☐ not a difficulty
- ☐ a moderate difficulty
- ☐ an important difficulty
- ☐ do not know
- ☐ not applicable

Question 37 Accessing tax information and contacting tax officials are:

- ☐ not a difficulty
- ☐ a moderate difficulty
- ☐ an important difficulty
- ☐ do not know
- ☐ not applicable

Question 38 Record keeping requirements are:

- ☐ not a difficulty
- ☐ a moderate difficulty
- ☐ an important difficulty
- ☐ do not know
- ☐ not applicable

Question 39 Audits and litigation are:

- ☐ not a difficulty
- ☐ a moderate difficulty
- ☐ an important difficulty
- ☐ do not know
- ☐ not applicable

IV-1 Transfer Pricing

Question 40 Has an EU tax administration examined your firm's cross-border intra-group transactions ("transfer pricing") in the past 5 years?

☐ No

☐ Yes

Questions 41-43 are only asked to companies that responded "Yes" to Question 40.

Company Taxation - Transfer Pricing Obstacles

Question 41 Regarding transfer pricing, dealing with documentation requirements is:

☐ not a difficulty

☐ a moderate difficulty

☐ an important difficulty

☐ do not know

☐ not applicable

Question 42 Regarding transfer pricing, dealing with the risk of double taxation is:

☐ not a difficulty

☐ a moderate difficulty

☐ an important difficulty

☐ do not know

☐ not applicable

Question 43 Regarding transfer pricing, dealing with procedures for dispute resolution is:

☐ not a difficulty

☐ a moderate difficulty

☐ an important difficulty

☐ do not know

☐ not applicable

IV-2 Company Taxation - Mergers and Acquisitions

Question 44 Has your firm merged with or acquired another business(es) in the EU during the past 5 years?

☐ No

☐ Yes

Questions 45-47 are only asked to companies that responded "Yes" to Question 44.

Tax Aspects of Mergers and Acquisitions

Question 45 Dealing with double taxation is:

- ☐ not a difficulty
- ☐ a moderate difficulty
- ☐ an important difficulty
- ☐ do not know
- ☐ not applicable

Question 46: Dealing with Capital Gains Taxes is:

- ☐ not a difficulty
- ☐ a moderate difficulty
- ☐ an important difficulty
- ☐ do not know
- ☐ not applicable

Question 47: Dealing with Transfer taxes is:

- ☐ not a difficulty
- ☐ a moderate difficulty
- ☐ an important difficulty
- ☐ do not know
- ☐ not applicable

V-1 Activities carried out without having a permanent establishment

Question 48 Does your firm carry out VAT taxable activities in another EU Member State without having a permanent establishment in that Member State but registered for VAT there?

- ☐ No
- ☐ Yes

Question 49 Does your firm have a tax representative or any kind of tax agent in this/these Member States?

- ☐ No
- ☐ Yes

Compliance with VAT obligations in another EU Member State

Question 50 Identification and registration is:

- ☐ not a difficulty
- ☐ a moderate difficulty
- ☐ an important difficulty
- ☐ do not know
- ☐ not applicable

Question 51 The frequency of VAT tax returns and listings is:

- ☐ not a difficulty
- ☐ a moderate difficulty
- ☐ an important difficulty
- ☐ do not know
- ☐ not applicable

Question 52 The complexity in VAT tax returns and listings is:

- ☐ not a difficulty
- ☐ a moderate difficulty
- ☐ an important difficulty
- ☐ do not know
- ☐ not applicable

Question 53 Invoicing requirements are:

- ☐ not a difficulty
- ☐ a moderate difficulty
- ☐ an important difficulty
- ☐ do not know
- ☐ not applicable

Question 54 Repayment and refund requirements are:

- ☐ not a difficulty
- ☐ a moderate difficulty
- ☐ an important difficulty
- ☐ do not know
- ☐ not applicable

Question 55 Accessing tax information and contacting tax officials are:

- ☐ not a difficulty
- ☐ a moderate difficulty
- ☐ an important difficulty
- ☐ do not know
- ☐ not applicable

Question 56 Record keeping requirements are:

- ☐ not a difficulty
- ☐ a moderate difficulty
- ☐ an important difficulty
- ☐ do not know
- ☐ not applicable

Question 57 Audits and litigation are:

- ☐ not a difficulty
- ☐ a moderate difficulty
- ☐ an important difficulty
- ☐ do not know
- ☐ not applicable

VAT compliance implications

Question 58 is only asked to companies that responded "No" to Question 48.

Question 58 Are VAT compliance requirements the reason why your firm has not carried out VAT taxable activities in another Member State (where it does not have a permanent establishment)?

- ☐ No
- ☐ Yes

V-2 Refunding of VAT

Question 59 Is your firm subject to VAT (which may be refundable under the 8th Directive) in another EU Member State in which it is not registered for VAT?

- ☐ No
- ☐ Yes

Question 60 is only asked to companies that responded "No" to Question 59.

Question 60 Refunds through the 8th Directive procedure are:

- ☐ not a difficulty
- ☐ a moderate difficulty
- ☐ an important difficulty
- ☐ do not know
- ☐ not applicable

Question 61 Have you ever not requested refunding because of the complexity or length of procedures?

- ☐ Yes
- ☐ No

VI Compliance costs

Question 62 Please estimate [in euros] the annual total worldwide compliance costs incurred when complying with the provisions of company taxation and VAT provisions.

Question 63 Please estimate the percentage of total annual compliance costs relating to domestic VAT compliance [in %].

Question 64 Please estimate the percentage of total annual compliance costs relating to domestic Company Taxation [in %].

Question 65 Please estimate the percentage of total annual compliance costs relating to other EU Member States' VAT compliance [in %].

Question 66 Please estimate the percentage of total annual compliance costs relating to other EU Member States' Company Taxation [in %].

Question 67 Please estimate the percentage of total annual compliance costs arising outside the EU [in %].

VII Taxes, Sales and Employment

Question 68 On the basis of your annual accounts, please indicate, in euros, the total tax on domestic income.

Question 69 On the basis of your annual accounts, please indicate, in euros, the total tax on income in other EU Member States.

Question 70 On the basis of your annual accounts, please indicate, in euros, the total tax on income in non-EU Member States.

Question 71 On the basis of your annual accounts, please indicate, in euros, your firm's total domestic sales (excluding VAT).

Question 72 On the basis of your annual accounts, please indicate, in euros, your firm's total sales (excluding VAT) in other EU Member States.

Question 73 On the basis of your annual accounts, please indicate, in euros, your firm's total sales (excluding VAT) for Non EU sales.

Question 74 Please estimate the proportion of your employees in your home Member State (in % of the total of employees).

Question 75 Please estimate the proportion of your employees in other EU Member States (in % of the total of employees).

Question 76 Please estimate the proportion of your employees outside the EU (in% of the total of employees).

VIII Investment Decisions and Company Taxation

Question 77 For a production plant?

- ☐ Never
- ☐ Sometimes
- ☐ Always
- ☐ Do not know
- ☐ Not applicable

Question 78 For a sales outlet?

- ☐ Never
- ☐ Sometimes
- ☐ Always
- ☐ Do not know
- ☐ Not applicable

Question 79 For a coordination centre?

- ☐ Never
- ☐ Sometimes
- ☐ Always
- ☐ Do not know
- ☐ Not applicable

Question 80 For a financial service centre?

- ☐ Never
- ☐ Sometimes
- ☐ Always
- ☐ Do not know

☐ Not applicable

Question 81 For a research and development centre?

☐ Never

☐ Sometimes

☐ Always

☐ Do not know

☐ Not applicable

VIII-2 Structure of international operations and company taxation

Question 82 Organise foreign operations through a subsidiary, branch or permanent establishment?

☐ Never

☐ Sometimes

☐ Always

☐ Do not know

☐ Not applicable

Question 83 Finance foreign operations locally, rather than directly or indirectly via the parent company?

☐ Never

☐ Sometimes

☐ Always

☐ Do not know

☐ Not applicable

Question 84 Use new equity or debt when financing foreign operations directly or indirectly via the parent company?

☐ Never

☐ Sometimes

☐ Always

☐ Do not know

☐ Not applicable

Question 85 Route income flowing to or from foreign operations through holding companies or through intermediaries in a third country?

☐ Never

- ☐ Sometimes
- ☐ Always
- ☐ Do not know
- ☐ Not applicable

Question 86 Use local borrowing, local equity issues or retained earnings, when financing foreign operations locally?

- ☐ Never
- ☐ Sometimes
- ☐ Always
- ☐ Do not know
- ☐ Not applicable

VIII-3 Other issues concerning investment

Question 87 When taking investment decisions, does your firm produce investment appraisal calculations on ...?

- ☐ a pretax basis
- ☐ a post tax basis
- ☐ it depends
- ☐ not applicable

Question 88 When taking internal management decisions concerning the corporate structure of your firm, such as establishing new subsidiaries, branches or permanent establishments, is approval from your tax department or tax advisors required?

- ☐ Yes, always
- ☐ Yes, sometimes
- ☐ Not applicable
- ☐ No, never
- ☐ Do not know

Question 89 The data provided in this questionnaire covers:

- ☐ All lower branches and subsidiaries of your company
- ☐ Does not cover any lower branches and subsidiaries
- ☐ Only some lower branches and subsidiaries of your company

Question 90 Did you encounter difficulties when completing this questionnaire?

☐ No

☐ Yes

ANNEX B – EUROPEAN BUSINESS TEST PANEL

The European Business Test Panel (EBTP) allows the Commission to contact and obtain the views of businesses located in the Community whenever major Commission legislative proposals and/or policy initiatives are being considered. The EBTP is entirely Internet based and using the on-line consultation tools developed under the Interactive Policy Making (IPM) initiative. It replaces the former Business Test Panel which operated as a pilot project over the last three years.

The EBTP is part of the Commission's overall policy to further improve and develop consultation links with businesses throughout the Community as it implements its "Better Regulation" Action Plan of June 2002. This is a key element of the European Union's drive of making Europe the best place to do business in the world. The EBTP will be an addition to - and not a substitute for - other existing consultation or impact assessment instruments used by the Commission.

In order to obtain a representative picture of the opinions of companies a target sample for the European Business Test Panel is constructed. The target sample is what would be the minimum required number of participants in a survey in order to obtain a representative view for the group of countries included (EU-15 plus Iceland and Norway). The target sample is constructed such that large companies are overrepresented. In the estimation account is taken of this over-representation by the use of sampling weights (see Annex D for the weighting process).

Table B-1 below indicates how the target sample is constructed.

Table B-1 Target Sample

Country	Sector	Company Size (number of employees)				Total
		0-9	10-49	50-249	250 or more	
Austria	Total Industry (excl. Construction)	3	8	11	12	34
	Construction	2	7	6	5	20
	Wholesale etc.	6	10	8	9	33
	Transport, storage and communication	2	4	6	13	25
	Financial intermediation	1	3	3	6	13
	Other Services	3	4	4	3	14
Belgium	Total Industry (excl. Construction)	4	9	8	14	35
	Construction	4	6	4	3	17
	Wholesale etc.	11	10	6	9	36
	Transport, storage and communication	3	5	4	8	20
	Financial intermediation	1	2	2	7	12
	Other Services	4	4	5	7	20
Germany	Total Industry (excl. Construction)	9	26	27	53	115
	Construction	9	22	14	11	56
	Wholesale etc.	18	29	18	32	97
	Transport, storage and	6	14	10	23	53

	communication					
	Financial intermediation	5	6	7	22	40
	Other Services	19	26	16	22	83
Denmark	Total Industry (excl. Construction)	3	7	8	11	29
	Construction	3	5	3	3	14
	Wholesale etc.	4	9	6	8	27
	Transport, storage and communication	2	3	3	4	12
	Financial intermediation	0	2	2	6	10
	Other Services	2	3	3	2	10
Spain	Total Industry (excl. Construction)	9	20	17	20	66
	Construction	10	15	10	8	43
	Wholesale etc.	18	19	13	15	65
	Transport, storage and communication	8	8	6	12	34
	Financial intermediation	4	3	4	13	24
	Other Services	9	10	9	10	38
Finland	Total Industry (excl. Construction)	3	6	7	11	27
	Construction	3	4	2	3	12
	Wholesale etc.	3	6	4	6	19
	Transport, storage and communication	2	3	3	7	15
	Financial intermediation	0	2	2	4	8
	Other Services	2	3	3	3	11
France	Total Industry (excl. Construction)	9	22	22	34	87
	Construction	11	16	10	11	48
	Wholesale etc.	16	23	16	20	75
	Transport, storage and communication	5	10	10	22	47
	Financial intermediation	3	4	6	17	30
	Other Services	14	13	13	11	51
Greece	Total Industry (excl. Construction)	3	7	7	7	24
	Construction	4	7	5	5	21
	Wholesale etc.	10	6	5	7	28
	Transport, storage and communication	2	3	3	2	10
	Financial intermediation	0	1	1	2	4
	Other Services	2	3	2	2	9
Ireland	Total Industry (excl. Construction)	1	5	7	7	20
	Construction	2	3	2	1	8
	Wholesale etc.	3	6	5	5	19
	Transport, storage and communication	1	2	2	5	10
	Financial intermediation	0	1	2	4	7
	Other Services	2	3	1	2	8
Iceland	Total Industry (excl. Construction)	1	2	1	2	6
	Construction	0	1	0	1	2
	Wholesale etc.	1	2	1	2	6
	Transport, storage and communication	0	1	0	2	3

Italy	Financial intermediation	0	1	0	1	2
	Other Services	0	1	1	4	6
	Total Industry (excl. Construction)	12	29	23	27	91
	Construction	11	14	7	6	38
	Wholesale etc.	18	18	10	13	59
	Transport, storage and communication	6	9	7	18	40
Luxembourg	Financial intermediation	4	4	5	15	28
	Other Services	12	8	6	6	32
	Total Industry (excl. Construction)	0	2	2	3	7
	Construction	1	2	2	1	6
	Wholesale etc.	2	3	2	1	8
	Transport, storage and communication	0	1	1	2	4
The Netherlands	Financial intermediation	0	2	2	3	7
	Other Services	1	1	1	1	4
	Total Industry (excl. Construction)	4	10	11	17	42
	Construction	5	6	7	5	23
	Wholesale etc.	9	13	10	14	46
	Transport, storage and communication	3	8	6	12	29
Norway	Financial intermediation	1	3	4	9	17
	Other Services	5	10	13	17	45
	Total Industry (excl. Construction)	3	7	8	11	29
	Construction	3	5	3	3	14
	Wholesale etc.	4	9	6	8	27
	Transport, storage and communication	2	3	3	4	12
Portugal	Financial intermediation	0	2	2	6	10
	Other Services	2	3	3	2	10
	Total Industry (excl. Construction)	5	13	13	12	43
	Construction	3	7	6	5	21
	Wholesale etc.	7	11	7	6	31
	Transport, storage and communication	2	4	3	7	16
Sweden	Financial intermediation	1	2	2	6	11
	Other Services	3	4	3	2	12
	Total Industry (excl. Construction)	3	7	9	14	33
	Construction	3	5	3	5	16
	Wholesale etc.	6	8	6	7	27
	Transport, storage and communication	3	4	4	9	20
United Kingdom	Financial intermediation	0	2	3	6	11
	Other Services	3	5	5	6	19
	Total Industry (excl. Construction)	9	19	23	37	88
	Construction	12	11	8	11	42
	Wholesale etc.	15	23	18	41	97
	Transport, storage and communication	7	9	8	22	46
	Financial intermediation	4	5	6	21	36

Other Services	14	18	15	30	77
Total	493	795	672	1032	2992

Table B-2 Company size used for sampling

Size class	Number of employees
1	0-9
2	10-49
3	50-249
4	250 and more

Table B-3 Sectors used for sampling

Sector	NACE codes	Description
1	Total industry (excluding construction)	C Mining and quarrying
		D Manufacturing
		E Electricity, gas and water supply
2	Construction	F45 Construction
3	Wholesale and retail trade, repair of motor vehicles, motorcycles and personal and household goods; hotels and restaurants	G Wholesale and retail trade; repair of motor vehicles, motorcycles and personal and household goods
		H Hotels and restaurants
4	Transport, storage and communication	I Transport, storage and communication
5	Financial intermediation	J Financial intermediation
6	Other services	K70 Real estate activities
		K71 Renting of machinery and equipment without operator and of personal and household goods
		K72 Computer and related activities
		K73 Research and development
		N85 Health and social work
		O90 Sewage and refuse disposal, sanitation and similar activities
		O92 Recreational, cultural and

	sporting activities
O93	Other service activities

Sampling Guidelines for National Co-ordinators

National co-ordinators played a central role in finding the participants to the European Business Test Panel. Below abstracts of the guidelines that were given to national coordinators in the Member States are presented.

"These sampling guidelines are intended to help national co-ordinators and business federations to set up the Business Test Panel in accordance with the matrix of companies as devised by Eurostat. They are deliberately put in non-technical terms.

Careful selection is essential in order to ensure that the Standing Panel is broadly representative of the Union's business population and to reduce the risk of introducing bias in panel membership. This means that certain selection techniques or practices such as self selection or purely voluntary participation should be avoided.

Member States in IMAC have expressed a preference for applying a sampling method which is practical and the least resource-intensive. Indeed, a large number of IMAC delegations wish to continue to work with national business organisations (NBOs), which they regard as a more efficient way to reach out to their companies. It was also felt that working through such NBOs increases credibility and results in higher participation levels.

The first question that arises when NBOs are used in setting up the Panel is whether they are sufficiently representative of the industry as a whole or of a particular sector. The national co-ordinators should select NBOs in such a way that all subsectors are covered and the distribution of its members reflect the population distribution.

If NBOs have lists of members (preferably in electronic form) and are prepared to release their membership list(s) for the purpose of creating the Standing EBTP, national co-ordinators could themselves exploit these lists with a view to conducting a random selection. In the event that NBOs themselves wish to conduct the sampling (perhaps because they would not want to release their membership lists), they will need to be given precise guidance on how to go about this. In this case, national co-ordinators would also need to be assured that the sampling method is applied correctly and to retain some degree of control over the end result.

In the case of one NBO whose membership is cross-sectoral and non-size specific (e.g. national chamber of commerce), its membership list would have to be split up according to industry sector and size as provided for in the matrix. This would result in 21 different combinations (i.e. 7 industry sectors combined with 3 size categories). If there are several NBOs each providing their own lists which together cover the entire population, these lists could be merged into one and then subdivided as above. For NBOs which only cover specific industry sectors (e.g. the national construction federation), its membership list could be split up according to size (i.e. 10-49, 50-249 and those with more than 250 employees). The same should be done for the other business sectors until all sectors are covered.

When the lists are drawn up, two methods can be used to select a sample.

1. Use a random number

Each of these 21 lists should contain the population from which the sample of companies will be drawn while the matrix indicates the number required from that list. By way of example, let us assume that a list contains 120 companies and the matrix requires 20, then the random number to be selected would be 6. The NBO or national co-ordinator will then proceed to select every 6th company on that list.

2. Sort the list at random

Using the above example of the list with 120 companies, sort the list at random and then take the first 20 which emerge from this exercise.

Further explanations and technical issues in the selection process were discussed under the supervision of the Internal market Directorate-general in the preparatory work to the launch of the European Business Test Panel.

For the purpose of the Company Tax Survey, it is important to stress that companies participating in the EBPT were not informed before of the fact that there would be a tax survey.

However, beyond these methodological elements, some national biases due to the specific selection of companies at national level are still possible. Furthermore, among firms that are members of the EBTP, only one-third participated in the Company Tax Survey. It is not excluded that firms which participated have more interest into the matter than non-participants, which could lead to some additional biases.

ANNEX C - RESPONSE

This Annex presents the responses for the different countries and considered topics in this paper.

Imputation company size for some Danish companies

For 13 Danish companies the size of the company was missing. For those companies values were imputed based on predictions using information of the other 136 Danish companies for which observations on company size were available. The predictions were based on the estimates of a regression model. The regression model was an ordered probit model that models the four company size categories (0-9 employees, 10-49 employees, 50-249 employees, more than 250 employees) as a function of company type (independent, parent, subsidiary), number of subsidiaries in home state, number of subsidiaries in other EU member state and location of parent company. The predicted company size values for the 13 Danish companies were exactly the same when an ordered logit model was estimated.

Country representation

Table C-1 Countries with respondents: domestic company taxation and VAT domestic context (sections 3.2.1 and 3.3.1)

Country	Micro	Small	Medium	Large	Total
Austria	-	2	9	20	31
Belgium	6	-	-	5	11
Denmark	53	31	49	16	149
Germany	3	10	12	52	77
Greece	-	3	-	-	3
Spain	-	-	3	6	9
Finland	7	12	6	18	43
France	2	0	0	0	2
Ireland	5	5	8	4	22
Italy	15	29	13	3	60
The Netherlands	13	23	26	47	109
Portugal	3	7	11	28	49
Sweden	4	6	5	10	25
United Kingdom	21	17	23	45	106
	132	145	165	254	696

Table C-2 Countries with respondents: 8th Directive (section 3.3.4)

Country	SME	Large	Total
Austria	6	11	17
Belgium	-	-	-
Denmark	25	8	33
Germany	6	23	29
Greece	-	-	-
Spain	-	2	2
Finland	4	8	12
France	-	-	-
Ireland	2		2
Italy	5		5
The Netherlands	16	21	37
Portugal	-	13	13
Sweden	2	4	6
United Kingdom	16	18	34
	82	108	190

Table C-3 Countries with respondents: Investing in other Member States – companies with a subsidiary, branch or permanent establishment (sections 3.2.2, 3.3.2, 3.4.2 and 3.4.4)

Country	SME	Large	Total
Austria	2	6	8
Belgium	-	4	4
Denmark	22	4	26
Germany	3	31	34
Greece	1		1
Spain	-	2	2
Finland	2	9	11
France	-	-	-
Ireland	3	3	6
Italy	3	1	4
The Netherlands	6	22	28
Portugal	1	5	6
Sweden	2	4	6
United Kingdom	6	22	28
	51	113	164

Table C-4 Countries with respondents of large companies (sections 3.2.4, 3.3.3 and 3.4.3)

Country	Transfer Pricing (section 3.2.4)	VAT issues for firms registered in another EU Member State where they don't have a Permanent Establishment (section 3.3.3)	Mergers and Acquisitions (section 3.4.3)
Austria	7	6	7
Belgium	3	-	2
Denmark	4	-	4
Germany	25	19	22
Greece	-	-	-
Spain	-	-	-
Finland	5	6	7
France	-	-	-
Ireland	-	-	3
Italy	-	-	2
The Netherlands	14	13	15
Portugal	-	3	-
Sweden	2	-	4
United Kingdom	13	10	3
	73	57	21
			90

ANNEX D - WEIGHTING

The responses are weighted by the number of companies in a country-company size cell. The number of companies in the population used for the weighting process for each country-company size cell is given in Table D-1 below.

Table D-1 Companies in population used for weighting

	Micro	Small	Medium	Large	Total
Austria	172121	23604	4210	837	200772
Belgium	422025	20785	3024	909	446743
Denmark	130459	13083	2341	489	146372
Germany	2562394	306674	38371	9966	2917405
Greece	677653	15180	2190	352	695375
Spain	2019033	103088	12829	2152	2137102
Finland	166914	9428	1618	482	178442
France	1985346	119118	20023	4213	2128700
Ireland	58498	8180	1414	254	68346
Italy	3191233	153461	14448	2394	3361536
The Netherlands	415750	38632	8406	2053	464841
Portugal	554503	33762	5343	741	594349
Sweden	179612	18199	3172	790	201773
United Kingdom	2674570	135980	21330	5905	2837785
Total	15210111	999174	138719	31537	16379541

Source: Eurostat (2001)

Table D-1 shows that the number of large companies in Portugal is about three times the number of large companies in Ireland. Suppose we have the same number of large companies responding for Ireland and Portugal. The weighting procedure implies that the responses given by Portuguese large companies receive three times as much weight than the responses of large Irish companies. The methodology used for the weighting procedure is outlined below.

We assume there are L country-company size cells. N_h denotes the number of companies in the population in country-company size cell h . n_h denotes the number of responding companies in country-company size cell h . The weight used for company i in country company size cell h is indicated by w_{hi} and is given by:

$$w_{hi} = \frac{N_h}{n_h}$$

If y is our variable of interest, say compliance costs, the total of Y is estimated as:

$$\hat{Y} = \sum_{h=1}^L \sum_{i=1}^{n_h} w_{hi} y_{hi} \quad (1)$$

With $z_{yhi} = w_{hi}y_{hi}$ and $\bar{z}_{yh} = \frac{1}{n_h} \sum_{i=1}^{n_h} z_{yhi}$ the variance of \hat{Y} is estimated by:

$$\hat{V}(\hat{Y}) = \sum_{h=1}^L \frac{n_h}{n_h - 1} \sum_{i=1}^{n_h} (z_{yhi} - \bar{z}_{yh})^2$$

If the interest is in the ratio of Y to X, say compliance costs in terms of sales, then the ratio is estimated as:

$$\hat{R} = \frac{\hat{Y}}{\hat{X}} \quad (2)$$

with \hat{Y} and \hat{X} calculated as in (1).

If we define $d_{hi} = \frac{y_{hi} - \hat{R}x_{hi}}{\hat{X}}$, $z_{dhi} = w_{hi}d_{hi}$ and $\bar{z}_{dh} = \frac{1}{n_h} \sum_{i=1}^{n_h} z_{dhi}$ the variance of \hat{R} is estimated as:

$$\hat{V}(\hat{R}) = \sum_{h=1}^L \frac{n_h}{n_h - 1} \sum_{i=1}^{n_h} (z_{dhi} - \bar{z}_{dh})^2$$

The estimation of a mean is equivalent to estimating a ratio with $x_{hi} = 1$ for all i and h . It can be verified that \bar{Y} , the estimated mean of y , is given by:

$$\bar{Y} = \sum_{h=1}^L \frac{N_h}{N} \frac{1}{n_h} \sum_{i=1}^{n_h} y_{hi}$$

The mean compliance costs in Chapter 2 are estimated in this way. The compliance costs in terms of taxes and sales in Chapter 2 are calculated as indicated by (2).

If y_{hi} is a 0/1 variable the proportion of y equal to one is estimated by estimating the mean of y (hence with $x_{hi} = 1$ for all i and h). The percentages presented in chapter 3 on the qualitative answers are calculated in this way.

For a subpopulation S the means, proportions and ratios are estimated in a similar way with y_{hi} and x_{hi} replaced by y_{hi}^* , respectively x_{hi}^* which are defined as:

$$y_{hi}^* = I_{(h,i) \in S} y_{hi}$$

$$x_{hi}^* = I_{(h,i) \in S} x_{hi}$$

The function $I_{(h,i) \in S}$ is the indicator function that indicates whether company i in stratum h belongs to the subpopulation S or not.

The percentages in Chapter 2 and Chapter 3 which are presented in boldface letter type are estimated percentages which are more than 1.96 its estimated standard deviation. The standard deviation is obtained as the square root of the calculated variance of the estimated mean, proportion or ratio (where appropriate). This is equivalent to testing whether the estimated mean, proportion or ratio is significantly different from zero at a level of significance equal to 5% (Cochran (1977)).

ANNEX E – COMPLIANCE COSTS

This Annex provides background information on the responses with respect to questions 62–67 that ask respondents to provide information on compliance costs.

Questions related to compliance costs

Respondents received some guidance with respect to the type of compliance costs they could include in their estimate.

"We give below an indication of the type of compliance costs your firm may have to meet.

Compliance costs include: all the costs related to complying with tax rules and obligations both within and outside the company (e.g. external consultants), in particular, the costs of acquiring information on tax laws and practices, tax obligations (registering, declaration, invoicing, payments and refunds), tax accounting, including tax lawyers, consulting firms, tax audit and litigation. Compliance costs can include salaries (including social security and fringe benefits) or non-personnel costs (e.g. computers). The costs can be incurred within or outside your tax department.

Compliance costs do not include: costs for maintaining or developing a financial accounting system, a management accounting and reporting system or an information system.

As to majority holdings, compliance costs are included for 100%. As to minority holdings, compliance costs are not included."

Question 62 Please estimate [in euros] the annual total worldwide compliance costs incurred when complying with the provisions of company taxation and VAT provisions

"The next five questions ask you to estimate the percentages of the total worldwide company taxation and VAT compliance costs in the previous question that relate to:

- *domestic VAT*
- *domestic company taxation*
- *other EU VAT*
- *other EU company taxation*
- *any non EU tax related compliance costs included in your total annual worldwide compliance costs in the previous question"*

Question 63 Please estimate the percentage of total annual compliance costs relating to domestic VAT compliance [in %].

Question 64 Please estimate the percentage of total annual compliance costs relating to domestic Company Taxation [in %].

Question 65 Please estimate the percentage of total annual compliance costs relating to other EU Member States' VAT compliance [in %].

Question 66 Please estimate the percentage of total annual compliance costs relating to other EU Member States' Company Taxation [in %].

Question 67 Please estimate the percentage of total annual compliance costs arising outside the EU [in %].

The total of the percentages given in Questions 63-67 should equal 100%.

Response on Compliance Costs

Of the 700 respondents 598 respondents provided an estimate of their total compliance costs. For 102 respondents zero total compliance costs are observed.

Table E-1 shows a cross-tabulation of compliance costs and taxes. The taxes are calculated as the sum of the reported amounts of taxes in questions 68-70. It shows that 136 respondents reported zero taxes. Of the 102 respondents with zero reported total compliance costs, 68 respondents report a positive amount of taxes.

Table E-1 Reported total compliance costs and taxes

Total compliance costs (euros)	Total taxes (euros)			Total
	Smaller than zero	Zero	Larger than zero	
Zero	0	34	68	102
Larger than zero	2	102	494	598
Total	2	136	562	700

Table E-2 shows a cross-tabulation of compliance costs and sales. The sales are calculated as the sum of the reported amounts of taxes in questions 71-73. Of the 102 respondents with zero reported total compliance costs, 78 respondents report a positive amount of sales. Table E-2 further shows that 65 respondents reported zero sales.

Table E-2 Reported total compliance costs and sales

Total compliance costs (euros)	Total sales (euros)			Total
	Smaller than zero	Zero	Larger than zero	
Zero	1	23	78	102
Larger than zero	0	42	556	598
Total	1	65	634	700

Respondents have been asked to provide a split of total compliance costs into VAT and company taxation compliance costs while distinguishing between domestic and EU compliance. Tax compliance costs outside the EU are the fifth category. A correct split is provided if the proportions of compliance costs for the five categories add up to 100%. For some respondents, however, no split is provided (all five proportions equal zero) or the proportions do not add up to 100%. Table E-3 shows the response on the split of compliance costs and distinguishes between zero total compliance costs and positive compliance costs.

Table E-3 Response compliance costs

Total compliance costs (euros)	Sum CC Categories			Total
	Zero	100%	Positive % unequal to 100%	
Zero	69	22	11	102
Larger than zero	10	528	60	598
Total	79	550	71	700

Table E-3 shows that for 550 companies the sum of the reported proportions for the five compliance costs categories adds up to 100%. For 79 companies the (sum of the) proportions equals zero. The sum of the proportions adds up to a positive number unequal to 100% for 71 companies. Of the 102 respondents reporting zero total compliance costs, 33 respondents report a split of the total compliance costs for which the proportions add up to a positive percentage (hence unequal to 0%).

Missing Values

It can be argued that for these 33 respondents the reported zero compliance costs are probably missing values. In the same way the reported zero compliance costs of respondents that report taxes or sales could be argued to be missing values. Of the 102 respondents with zero compliance costs, 87 paid taxes, sold products/services or provided a split of the (zero) compliance costs over the five categories (this number is not reported in the tables). That suggests that at least 87 of the 102 observations with zero compliance costs are missing values. Throughout the analysis it is assumed that these missing values are missing at random.

Respondents that had difficulties with participating in the European Tax Survey

Respondents could indicate if they had difficulties with the questions. Of the 700 respondents, 525 reported to have had no difficulties with the questions in the European Tax Survey. In total 175 respondents indicated they had difficulties with some questions in the survey. Table E-4 shows that 34 of them reported zero compliance costs.

Table E-4 Reported difficulties with European Tax Survey

Total compliance costs (euros)	Difficulties:		
	Yes	No	Total
Zero	34	68	102
Larger than zero	141	457	598
Total	175	525	700

Additionally, an open question allowed respondents to make remarks about the difficulties they faced. Very often the respondents were small companies indicating that the questions were not relevant to them. Other remarks were by companies that stressed their particular situation (for example, some companies indicated ownership by persons). Careful investigation of the replies suggests that for 29 respondents the reported amounts on total compliance costs, taxes or sales could be wrong. Table E-5 shows the number of those respondents reporting zero and positive compliance costs.

Table E-5 Reported problems compliance costs, taxes and sales

Total compliance costs (euros)	<u>Problems with:</u> Compliance costs	Taxes	Sales	Compliance costs, taxes or sales
Zero	3	1	2	6
Larger than zero	12	7	6	23
Total	15	8	8	29

ANNEX F – REGRESSION ANALYSIS

The results presented in Chapter 2 are based on models that explain compliance costs or compliance costs in terms of sales by a set of company characteristics. The basic model that underlies those results is given in equation (1) below.

$$\log(\text{COMPLIANCE} - \text{COSTS}_i) = \beta * \text{CHARACTERISTICS}_i + \varepsilon_i \quad (1)$$

$\text{COMPLIANCE} - \text{COSTS}_i$ denotes the compliance costs of firm i and CHARACTERISTICS_i denotes the vector of company characteristics for firm i . The compliance costs are expressed in (natural) logarithms. The vector of parameters corresponding to the company characteristics is denoted by β . The parameter ε_i denotes the error term for company i .

The interpretation of the coefficients captured by vector β is the *relative* change in compliance costs due to an *absolute* change in the company characteristics. All the included company characteristics in the model are dummy variables which are equal to zero or one. This means that, by approximation, the coefficients can be interpreted as relative compliance costs differentials. For example, if $\text{CHARACTERISTIC}_{ik}$ is a dummy variable indicating whether a company has a subsidiary abroad or not, then the parameter β_k is the relative compliance costs differential between companies with a subsidiary abroad and companies without a subsidiary abroad, ceteris paribus (Verbeek (2004)).

If we use short notation C for the vector that contains the logarithm of compliance costs for all companies, and the matrix X to denote company characteristics of all companies, the model in (1) can be rewritten as:

$$C = X' \beta + \varepsilon$$

Un-weighted regression

$\hat{\beta}_{UW}$ denotes the un-weighted estimate of β which is obtained by ordinary least squares and given by:

$$\hat{\beta}_{UW} = (X' X)^{-1} X' C$$

$\hat{V}(\hat{\beta}_{UW})$ denotes the estimated covariance matrix of $\hat{\beta}_{UW}$ and is calculated as:

$$\hat{V}(\hat{\beta}_{UW}) = (X' X)^{-1} S_{UW} (X' X)^{-1}$$

with S_{UW} calculated as: $\sum_{h=1}^L \sum_{i=1}^{n_h} e_{hi} x_{hi} x'_{hi}$ with $e_{hi} = C_{hi} - x'_{hi} \hat{\beta}_{UW}$. L denotes the number of country-company size cells and n_h denotes the number of responses in

country company size cell h . S_{uw} is the estimated ordinary least squares covariance that assumes homoskedastic errors, while $\hat{V}(\hat{\beta}_{uw})$ is the estimated covariance matrix which is robust to heteroskedasticity of an unspecified form.

Weighted regression

$\hat{\beta}_w$ denotes the weighted estimate of β which is obtained by weighted ordinary least squares (WOLS) and given by:

$$\hat{\beta}_w = (X'WX)^{-1} X'WC$$

with W a diagonal matrix with the weights w_{hi} as elements.

The covariance matrix of the weighted estimate of β is estimated by:

$$\hat{V}(\hat{\beta}_w) = (X'WX)^{-1} S_w (X'WX)^{-1}$$

with

$$S_w = \sum_{h=1}^L \frac{n_h}{n_h - 1} \sum_{i=1}^{n_h} (z_{dhi} - \bar{z}_{dh})^2$$

and

$$e_{hi} = C_{hi} - x_{hi}' \hat{\beta}_w$$

$$d_{hi} = x_{hi}' e_{hi}$$

$$z_{dhi} = w_{hi} d_{hi}$$

$$\bar{z}_{dh} = \frac{1}{n_h} \sum_{i=1}^{n_h} z_{dhi}$$

Chapter 2 presents the estimation results for the different versions of the basic model in (1). The different models differ in the dependent variable (e.g. total compliance costs, company taxation compliance costs, VAT compliance costs expressed in euros and in terms of sales) and the included company characteristics.

Companies with non-zero compliance costs that did not indicate specific problems with questions on compliance costs and sales are included in the analysis. In addition, four companies that reported very low compliance costs (less than 10€) and one company that reported very high compliance costs (1.5 billion €) were excluded from the analysis. These reported compliance costs are unlikely to reflect the actual compliance costs and were frequently identified as outliers influencing the regression results by using the diagnostic tools in Belsley et. al. (1980). Whereas no sales were reported by a company and/or only one company reports for a certain company size-country cell fewer observations could be used in the weighted regressions and/or regressions in which compliance costs over sales is the dependent variable.

For all the regression results presented in Chapter 2 the following approach was taken. First, the model was estimated without using weights. Second, a test for the presence of a non-linear relationship between compliance costs and company characteristics was conducted using the estimates of the model. For this purpose a regression equation error specification test was conducted. The idea behind this test is that in the absence of misspecification higher powers of the predicted values of compliance costs, based on the estimated model, should not help in explaining the compliance costs. An auxiliary regression of a model that includes the square of the predicted compliance costs as an additional variable was estimated. For all the models presented in the main text the auxiliary regressions did not indicate misspecification.

The third step involved was a test to investigate whether a weighted regression would be more appropriate compared to an un-weighted regression. The test suggested by Dumouchel and Duncan (1983) was used. It is an omitted-variable test, which tests whether the sample weight and all its interactions with the company characteristics that are included in the model are of additional explanatory value to the model. The test requires an auxiliary regression that includes the sample weight and its interactions with company characteristics in the model in addition to the original company characteristics included in the model.

For all the models that are presented in the text this test was conducted. In all cases the test rejected the hypothesis that the coefficients of the additional variables related to the sample weight are jointly equal to zero. It suggests that the use of weights would improve our understanding of compliance costs and their relation with company characteristics.

Therefore, the weighted estimates form the basis of the compliance cost analysis. The models using weights were estimated after deletion of country-company size cells for which only one observation was available. The weighted estimates were obtained by using weighted ordinary least squares (WOLS).

The full set of estimated coefficients for all models is presented below. In addition to the weighted regression results, the results of the un-weighted regressions are also presented for comparison. These are estimates obtained by using ordinary least squares (OLS).

Total compliance costs

The number of responses per country included in the weighted regression that explains the absolute total compliance costs are presented in Table F-1 below.

Table F-1 Number of responses used for estimates total compliance costs

Country	Absolute total compliance costs	Relative total compliance costs
Austria	26	25
Belgium	10	10
Denmark	118	103
Germany	62	55
Greece	2	2
Spain	8	8
Finland	38	36
France	-	-
Ireland	20	19
Italy	43	41
The Netherlands	94	88
Portugal	33	33
Sweden	16	15
United Kingdom	102	99
	572	534

Table F-2 Total compliance costs – weighted results

Dependent variable	Model 1	Model 2	Model 3	Model 4
	Compliance costs (1000 euros)	Compliance costs (1000 euros)	Compliance costs/sales	Compliance costs/sales
Company characteristics				
Small	0.585 (0.553)	0.581 (0.552)	-0.194 (0.539)	-0.197 (0.540)
Medium	1.349** (0.606)	1.324** (0.609)	-1.645** (0.650)	-1.670** (0.648)
Large	2.176*** (0.754)	1.974*** (0.702)	-2.695*** (0.698)	-2.201*** (0.656)
Parent with subsidiary/branches/permanent establishments in Home State	0.306 (0.297)	0.290 (0.298)	-0.250 (0.372)	-0.273 (0.376)
Parent with subsidiary/branches/permanent establishments in other Member States	1.679*** (0.583)	-	0.715 (0.601)	-
Sub/branch/PE in other Member States: 1-5	-	1.891** (0.777)	-	1.260** (0.535)
Sub/branch/PE in other Member States: 6-15	-	2.130*** (0.412)	-	0.328 (0.621)
Sub/branch/PE in other Member States: 16-50	-	3.490*** (0.948)	-	-3.053** (1.316)

Sub/branch/PE in other Member States:	-	0.588 (0.657)	-	-0.629 (0.835)
>50				
Manufacturing	-0.044 (0.483)	0.001 (0.471)	0.681 (0.567)	0.681 (0.586)
Electricity, Gas and water supply	0.617 (0.490)	0.658 (0.472)	-0.057 (0.843)	-0.115 (0.891)
Construction	0.559 (0.680)	0.567(0.668)	0.575 (0.870)	0.505 (0.855)
Wholesale and retail trade	0.169 (0.716)	0.217 (0.709)	-0.623 (0.797)	-0.628 (0.809)
Hotels, restaurants and bars	-0.281 (0.904)	-0.381 (0.925)	4.836*** (1.504)	4.640*** (1.529)
Transport, storage and communication	0.467 (0.887)	0.493 (0.878)	-0.064 (1.058)	-0.052 (1.066)
Financial intermediation	0.571 (1.083)	0.548 (1.068)	-0.564 (0.817)	-0.850 (0.808)
Real estate, renting and business activities	-0.536 (0.922)	-0.508 (0.917)	1.561 (0.917)	1.557* (0.931)
Health and social work	-0.782 (0.879)	-0.508 (0.917)	1.235 (0.956)	1.262 (0.968)
Other community, social and personal activities	-0.529 (0.812)	-0.492 (0.805)	0.922 (0.853)	0.923 (0.858)
Belgium	0.415 (0.752)	0.394 (0.736)	-0.647 (0.958)	-0.494 (0.987)
Denmark	1.270* (0.671)	1.174* (0.663)	0.335 (1.027)	0.704 (1.055)
Germany	0.563 (0.633)	0.528 (0.644)	0.096 (0.905)	0.193 (0.942)
Greece	-1.218 (0.796)	-1.332 (0.907)	1.204 (0.909)	1.043 (0.856)
Spain	2.086 (0.919)	2.119 (0.928)	0.689 (1.947)	0.762 (1.972)
Finland	0.014 (1.549)	0.151 (1.591)	-1.670 (0.947)	-1.333 (1.158)
Ireland	1.160 (0.840)	1.138 (0.835)	1.322 (1.127)	1.508 (1.161)
Italy	1.670** (0.688)	1.637** (0.688)	0.161 (0.947)	0.259 (0.977)
The Netherlands	-0.287 (0.644)	-0.170 (0.665)	0.425 (1.016)	0.705 (1.049)
Portugal	0.071 (0.601)	0.071 (0.615)	-0.404 (1.089)	0.253 (1.126)
Sweden	0.058 (0.634)	0.019 (0.636)	0.516 (0.860)	0.610 (0.898)
United Kingdom	0.340 (0.531)	0.290 (0.535)	0.255 (0.860)	0.305 (0.895)
2003	-0.002 (0.304)	0.011 (0.305)	0.545 (0.460)	0.563 (0.465)
Adjusted R ²	0.267	0.267	0.240	0.250
Observations	572	572	534	534

- Notes: i) Estimation method: Weighted OLS with constant included.
ii) ***, **, *, denote, respectively, significance at 1, 5, 10% level.
iii) Standard deviations of the coefficients are in parentheses and robust against any form of heteroskedasticity.
iv) Compliance costs and its relative burden are in logarithms. Zero observations on compliance costs have been excluded.

Table F-3 Total compliance costs – un-weighted results

	Model 1	Model 2	Model 3	Model 4
Dependent variable	Compliance costs (1000 euros)	Compliance costs (1000 euros)	Compliance costs/Sales	Compliance costs/Sales
Company characteristics				
Small	0.324 (0.303)	0.402 (0.302)	-0.518 (0.332)	-0.533 (0.332)
Medium	0.848*** (0.255)	0.928*** (0.256)	-1.226*** (0.355)	-1.245*** (0.352)
Large	1.844*** (0.246)	1.824*** (0.244)	-2.354*** (0.355)	-2.335*** (0.353)
Parent with subsidiary/branches/ permanent establishments in Home State	0.205 (0.207)	0.177 (0.207)	-0.737 (258)	
Parent with subsidiary/branches/ permanent establishments in other Member States	1.584*** (0.179)	-	0.191 (0.221)	
Sub/branch/PE in other Member States: 1-5	-	1.004*** (0.179)	-	0.179 (0.238)
Sub/branch/PE in other Member States: 6-15	-	2.230*** (0.423)	-	0.715 (0.492)
Sub/branch/PE in other Member States: 16-50	-	2.812*** (0.437)	-	-0.713 (0.468)
Sub/branch/PE in other Member States: >50	-	2.439*** (0.517)	-	0.557 (0.601)
Manufacturing	-0.763** (0.382)	-0.948** (0.385)	-0.476 (0.423)	-0.546 (0.441)
Electricity, Gas and water supply	-0.515 (0.417)	-0.578 (0.431)	-1.001 (0.609)	-1.100* (0.655)
Construction	-0.437 (0.442)	-0.533 (0.450)	0.085 (0.544)	-0.007 (0.560)
Wholesale and retail trade	-0.952** (0.393)	-1.157** (0.402)	-1.715*** (0.457)	-1.794*** (0.478)
Hotels, restaurants and bars	-1.307*** (0.449)	-1.336*** (0.457)	0.177 (0.713)	0.092 (0.725)
Transport, storage and communication	-1.083** (0.423)	-1.260*** (0.427)	-0.868 (0.528)	-0.997* (0.548)
Financial intermediation	-0.685 (0.421)	-0.734* (0.431)	-1.249*** (0.474)	-1.379*** (0.493)
Real estate, renting and business activities	-1.360*** (0.380)	-1.468*** (0.390)	-0.263 (0.458)	-0.365 (0.476)
Health and social work	-1.675*** (0.482)	-1.778*** (0.488)	-1.460** (0.691)	-1.553** (0.705)
Other community, social	-1.281** (0.482)	-1.384*** (0.488)	-0.581 (0.691)	-0.696 (0.705)

and personal activities	(0.498)	(0.509)	(0.462)	(0.483)
Belgium	-0.127	-0.127	-0.345	-0.211
	(0.508)	(0.457)	(0.753)	(0.750)
Denmark	0.354	0.262	0.182	0.230
	(0.335)	(0.336)	(0.398)	(0.400)
Germany	0.534	0.339	-0.308	-0.224
	(0.348)	(0.339)	(0.362)	(0.370)
Greece	-1.118**	-0.878**	1.618***	1.692***
	(0.469)	(0.383)	(0.534)	(0.555)
Spain	-1.078*	1.152**	-0.016	0.025
	(0.637)	(0.620)	(1.246)	(1.245)
Finland	-0.719*	-0.875**	-0.602	-0.561
	(0.457)	(0.443)	(0.449)	(0.452)
Ireland	0.190	0.120	0.550	0.617
	(0.464)	(0.494)	(0.791)	(0.757)
Italy	1.030**	0.973**	0.414	0.453
	(0.440)	(0.440)	(0.495)	(0.496)
The Netherlands	0.007	-0.109	0.171	0.198
	(0.327)	(0.325)	(0.368)	(0.369)
Portugal	0.567	0.585	0.615	0.641
	(0.469)	(0.462)	(0.533)	(0.539)
Sweden	-0.273	-0.287	0.370	0.472
	(0.451)	(0.422)	(0.413)	(0.429)
United Kingdom	-0.033	-0.111	0.200	0.252
	(0.325)	(0.322)	(0.352)	(0.352)
2003	0.201	0.245	0.517*	0.523*
	(0.370)	(0.222)	(0.270)	(0.270)
Adjusted R ²	0.335	0.363	0.236	0.241
Observations	572	572	534	534

- Notes:
- i) Estimation method: Weighted OLS with constant included.
 - ii) ***, **, *, denote, respectively, significance at 1, 5, 10% level.
 - iii) Standard deviations of the coefficients are in parentheses and robust against any form of heteroskedasticity.
 - iv) Compliance costs and its relative burden are in logarithms. Zero observations on compliance costs have been excluded.

For the un-weighted results, the reported standard errors are robust to heteroskedasticity of an unknown form (also known as White-standard errors).

Company Taxation Compliance Costs

Table F-4 Number of responses used for estimates company taxation compliance costs

Country	Absolute company taxation compliance costs	Relative company taxation compliance costs
Austria	24	23
Belgium	9	9
Denmark	105	90
Germany	50	45
Greece	-	-
Spain	6	6
Finland	35	33
France	-	-
Ireland	35	14

Italy	31	30
The Netherlands	65	61
Portugal	27	27
Sweden	14	13
United Kingdom	96	93
	477	444

Table F-5 Company taxation compliance costs – weighted results

	Model 1	Model 2	Model 3	Model 4
Dependent variable	Compliance costs (1000 euros)	Compliance costs (1000 euros)	Compliance costs/sales	Compliance costs/sales
Company characteristics				
Small	0.030 (0.595)	0.051 (0.591)	-0.333 (0.658)	-0.343 (0.649)
Medium	0.786 (0.716)	0.767 (0.730)	-1.752** (0.859)	-1.819** (0.879)
Large	1.406** (0.601)	1.292** (0.591)	-2.222*** (0.798)	-1.961** (0.793)
Transfer Pricing	1.022** (0.496)	0.856* (0.476)	0.091 (0.762)	-0.098 (0.667)
Merger	0.616* (0.365)	0.575 (0.375)	0.888* (0.488)	0.918* (0.498)
Parent with subsidiary/branches/permanent establishments in Home State	-0.017 (0.484)	-0.033 (0.488)	-0.557 (0.621)	-0.568 (0.622)
Parent with subsidiary/branches/permanent establishments in other Member States	1.530*** (0.478)	-	-1.078** (0.560)	-
Sub/branch/PE in other Member States: 1-5	-	1.814*** (0.678)	-	-0.636 (0.757)
Sub/branch/PE in other Member States: 6-15	-	1.626*** (0.537)	-	0.275 (0.700)
Sub/branch/PE in other Member States: 16-50	-	2.723*** (1.083)	-	-3.832* (1.548)
Sub/branch/PE in other Member States: >50	-	1.220 (0.834)	-	-1.390 (0.850)
Manufacturing	-0.702 (0.598)	-0.667 (0.593)	0.306 (0.676)	0.257 (0.681)
Electricity, Gas and water supply	0.271 (0.772)	-0.212 (0.775)	-0.728 (1.078)	-0.822 (1.095)
Construction	-0.261**	-0.257	0.081	-0.009

	(0.664)	(0.672)	(0.843)	(0.846)
Wholesale and retail trade	-1.208	-1.185	-1.786	-1.857
	(0.900)	(0.902)	(1.150)	(1.160)
Hotels, restaurants and bars	-0.845	-0.836	-1.148	-1.207
	(1.117)	(1.092)	(1.073)	(1.057)
Transport, storage and communication	-0.068	-0.058	-1.754	-1.815
	(1.141)	(1.138)	(1.375)	(1.370)
Financial intermediation	0.443	0.369	-0.496	-0.822
	(0.862)	(0.842)	(1.088)	(1.120)
Real estate, renting and business activities	-2.255***	-2.206***	-0.160	-0.197
	(0.762)	(0.760)	(0.951)	(0.952)
Health and social work	-1.760*	-1.733*	0.332	0.279
	(0.964)	(0.959)	(1.212)	(1.208)
Other community, social and personal activities	-1.702*	-1.658*	-0.196	-0.229
	(0.904)	(0.908)	(1.027)	(1.023)
Belgium	0.848	0.797	-1.151	-1.155
	(0.804)	(0.818)	(0.908)	(0.915)
Denmark	0.628	0.571	-0.450	0.221
	(0.710)	(0.713)	(0.916)	(0.906)
Germany	0.750	0.691	-0.482	-0.471
	(0.863)	(0.869)	(0.974)	(0.971)
Spain	0.546	0.624	-2.469	-2.363
	(1.219)	(1.141)	(1.509)	(1.437)
Finland	0.083	0.107	-2.126*	-2.037
	(2.099)	(2.107)	(1.220)	(1.211)
Ireland	-0.444	-0.424	-0.635	-0.462
	(0.708)	(0.728)	(1.465)	(1.529)
Italy	1.257	1.210	-1.018	-0.996
	(0.766)	(0.766)	(0.926)	(0.928)
The Netherlands	-1.383	-1.319*	0.310	0.440
	(0.725)	(0.743)	(1.048)	(1.057)
Portugal	-0.098	-0.116	-1.087	-0.984
	(0.976)	(0.974)	(0.966)	(0.968)
Sweden	-0.516	-0.550	-0.523	-0.480
	(0.798)	(0.802)	(0.877)	(0.882)
United Kingdom	0.331	0.282	-0.195	0.190
	(0.740)	(0.752)	(0.876)	(0.884)
2003	-0.097	-0.114	0.390	0.364
	(0.369)	(0.376)	(0.545)	(0.545)
Adjusted R ²	0.403	0.400	0.242	0.243
Observations	477	477	444	444

- Notes:
- i) Estimation method: Weighted OLS with constant included.
 - ii) ***, **, *, denote, respectively, significance at 1, 5, 10% level.
 - iii) Standard deviations of the coefficients are in parentheses and robust against any form of heteroskedasticity.
 - iv) Compliance costs and its relative burden are in logarithms. Zero observations on compliance costs have been excluded.

Table F-6 Company taxation compliance costs – un-weighted results

	Model 1	Model 2	Model 3	Model 4
Dependent variable	Compliance costs (1000 euros)	Compliance costs (1000 euros)	Compliance costs/sales	Compliance costs/sales
Company characteristics				
Small	0.094 (0.356)	0.167 (0.357)	-0.423 (0.380)	-0.443 (0.380)
Medium	1.632** (0.285)	0.659** (0.295)	-1.156*** (0.401)	-1.196*** (0.399)
Large	1.633** (0.285)	1.678** (0.285)	-1.909** (0.392)	-1.912*** (0.387)
Transfer Pricing	1.141*** (0.221)	0.923** (0.224)	-0.064 (0.308)	-0.002 (0.312)
Merger	0.509** (0.191)	0.399** (0.188)	-0.195 (0.246)	-0.137 (0.251)
Parent with subsidiary/branches/permanent establishments in Home State	0.096 (0.227)	0.089 (0.227)	-0.557 (0.621)	0.945 (0.294)
Parent with subsidiary/branches/permanent establishments in other Member States	1.260*** (0.199)		0.252 (0.247)	
Sub/branch/PE in other Member States: 1-5		0.879*** (0.203)		0.286 (0.257)
Sub/branch/PE in other Member States: 6-15		1.848*** (0.442)		0.600 (0.555)
Sub/branch/PE in other Member States: 16-50		2.231*** (0.473)		-0.861 (0.531)
Sub/branch/PE in other Member States: >50		2.014*** (0.498)		0.624 (0.626)
Manufacturing	-1.418*** (0.334)	-1.483*** (0.361)	-0.645* (0.369)	-0.718* (0.378)
Electricity, Gas and water supply	-1.255*** (0.443)	-1.230** (0.497)	-1.286* (0.722)	-1.407* (0.730)
Construction	-1.315*** (0.433)	-1.330*** (0.455)	-0.361 (0.531)	-0.439 (0.539)
Wholesale and retail trade	-1.588*** (0.360)	-1.675*** (0.393)	-1.914*** (0.414)	-1.986*** (0.422)
Hotels, restaurants and bars	-1.964*** (0.541)	-1.901*** (0.570)	-0.907 (0.549)	-1.024* (0.558)
Transport, storage and communication	-1.614*** (0.396)	-1.712*** (0.424)	-1.129** (0.529)	-1.338** (0.541)
Financial intermediation	-0.857** (0.386)	-0.845** (0.419)	-1.217*** (0.434)	-1.375*** (0.449)
Real estate, renting and business activities	-2.097*** (0.342)	-2.121*** (0.378)	-0.627 (0.447)	-0.755* (0.456)
Health and social work	-1.932*** (0.577)	-1.946*** (0.593)	-0.622 (0.671)	-0.732 (0.682)
Other community, social	-1.753***	-1.790***	-0.669	-0.792

and personal activities	(0.478)	(0.510)	(0.452)	(0.464)
Belgium	0.276	0.311	0.056	0.196
	(0.514)	(0.458)	(0.850)	(0.818)
Denmark	0.608	0.512	0.284	0.353
	(0.363)	(0.362)	(0.408)	(0.411)
Germany	0.615	0.441	-0.365	-0.237
	(0.380)	(0.379)	(0.399)	(0.411)
Spain	0.667	0.776	-0.333	-0.314
	(0.722)	(0.725)	(1.454)	(1.453)
Finland	-0.513	-0.664*	-0.716	-0.665
	(0.477)	(0.475)	(0.476)	(0.480)
Ireland	0.324	0.159	0.958	1.051
	(0.573)	(0.605)	(0.779)	(0.696)
Italy	1.441**	1.361**	0.492	0.542
	(0.439)	(0.443)	(0.501)	(0.501)
The Netherlands	0.056	-0.024	0.061	0.083
	(0.361)	(0.358)	(0.385)	(0.390)
Portugal	0.697	0.643	0.195	0.241
	(0.456)	(0.458)	(0.569)	(0.574)
Sweden	-0.260	-0.336	0.159	0.282
	(0.520)	(0.483)	(0.502)	(0.529)
United Kingdom	0.450	0.357	0.273	0.330
	(0.343)	(0.342)	(0.362)	(0.363)
2003	-0.111	-0.072	0.287	0.302
	(0.219)	(0.219)	(0.280)	(0.276)
Adjusted R ²	0.396	0.409	0.204	0.211
Observations	477	477	444	444

- Notes:
- i) Estimation method: Weighted OLS with constant included.
 - ii) ***, **, *, denote, respectively, significance at 1, 5, 10% level.
 - iii) Standard deviations of the coefficients are in parentheses and robust against any form of heteroskedasticity.
 - iv) Compliance costs and its relative burden are in logarithms. Hence, zero observations on compliance costs are excluded.

Table F-7 Company taxation compliance costs (models excluding transfer pricing and merger company characteristics) – weighted results

	Model 1	Model 2	Model 3	Model 4
Dependent variable	Compliance costs (1000 euros)	Compliance costs (1000 euros)	Compliance costs/sales	Compliance costs/sales
Company characteristics				
Small	0.133 (0.579)	0.139* (0.580)	-0.252 (0.661)	-0.256 (0.658)
Medium	0.975 (0.690)	0.912 (0.711)	-1.623 (0.836)	-1.717** (0.862)
Large	1.683*** (0.568)	1.430 (0.556)	-2.150*** (0.739)	-1.969** (0.754)
Parent with subsidiary/branches/permanent establishments in Home State	-0.000 (0.487)	-0.026 (0.491)	-0.542 (0.626)	-0.561 (0.627)

Parent with subsidiary/branches/ permanent establishments in other Member States	1.918 ^{***} (0.551)	-	-0.658 (0.545)	-
Subsidiaries in other Member States:	-	2.235 ^{**} (0.674)	-	-0.075 (0.705)
1-5				
Subsidiaries in other Member States:	-	2.420 ^{***} (0.532)	-	0.187 (0.619)
6-15				
Subsidiaries in other Member States:	-	3.666 ^{***} (0.815)	-	-3.034 ^{**} (1.487)
16-50				
Subsidiaries in other Member States:	-	1.396 [*] (0.801)	-	-1.087 (0.894)
>50				
2003	-0.007 (0.357)	-0.040 (0.366)	0.514 (0.543)	0.480 (0.545)
<i>Sectors (10)</i>	Yes ^{***}	Yes ^{***}	Yes ^{***}	Yes ^{***}
<i>Countries (11)</i>	Yes ^{***}	Yes ^{***}	Yes	Yes
Adjusted R ²	0.398	0.396	0.234	0.233
Observations	477	477	444	444

- Notes:
- i) Estimation method: Weighted OLS with constant included.
 - ii) ***, **, *, denote, respectively, significance at 1, 5, 10% level.
 - iii) Standard deviations of the coefficients are in parentheses and robust against any form of heteroskedasticity.
 - iv) Compliance costs and its relative burden are in logarithms. Hence, zero observations on compliance costs are excluded.

VAT Compliance Costs

Table F-8 Number of responses used for estimates VAT compliance costs

Country	Absolute VAT compliance costs	Relative VAT compliance costs
Austria	24	23
Belgium	7	7
Denmark	100	87
Germany	53	47
Greece	-	-
Spain	6	6
Finland	35	33
France	-	-
Ireland	15	14
Italy	33	32
The Netherlands		74
Portugal	79	27
Sweden	27	13
United Kingdom	14	
	94	92
	487	455

Table F-9 VAT compliance costs – weighted results

	Model 1	Model 2	Model 3	Model 4
Dependent variable	Compliance costs (1000 euros)	Compliance costs (1000 euros)	Compliance costs/sales	Compliance costs/sales
Company characteristics				
Small	-0.016 (0.425)	0.343 (0.382)	0.551 (0.616)	-0.322 (0.593)
Medium	0.581 (0.524)	0.796* (0.472)	-2.193*** (0.727)	-1.834*** (0.651)
Large	0.972** (0.454)	1.095** (0.452)	-3.472*** (0.747)	-2.976*** (0.693)
Parent with subsidiary/branches/ permanent establishments in Home State	0.710* (0.386)	0.718** (0.299)	0.062 (0.446)	0.182 (0.418)
Parent with subsidiary/branches/ permanent establishments in other Member States	1.768*** (0.398)	-	0.857 (0.902)	-
<u>Domestic Companies without a subsidiary, branch or permanent establishment in other Member States:</u>				
2. Only foreign VAT activities without physical presence	-	-2.519*** (0.415)	-	-0.844 (0.606)
3. Only VAT incurred on inputs abroad	-	-0.773 (0.384)	-	-1.413*** (0.621)
4. Both foreign VAT activities without physical presence and VAT incurred on inputs abroad		0.782** (0.305)		-0.210 (0.535)
<u>Companies with a subsidiary, branch or permanent establishment in other Member States:</u>				
5. No foreign VAT activities without physical presence and no VAT incurred on inputs abroad	-	1.260*** (0.448)	-	0.739 (1.170)
6. Only foreign VAT activities without physical presence	-	0.911 (1.476)	-	0.087 (1.212)
7. Only VAT incurred on inputs abroad	-	3.767*** (0.530)	-	0.743 (0.779)
8. Both foreign VAT activities without physical presence and VAT incurred on inputs abroad		3.374*** (0.970)		-0.845 (0.739)
Manufacturing	0.630 (0.553)	1.017 (0.652)	1.313 (0.671)	-1.574** (0.674)

Electricity, Gas and water supply	1.309** (0.623)	0.920 (0.683)	0.244 (0.919)	-0.038 (0.891)
Construction	-0.654 (0.616)	-0.673(0.700)	-0.764 (0.956)	-0.660 (0.952)
Wholesale and retail trade	0.747 (0.621)	0.706 (0.694)	-0.257 (0.819)	-0.212 (0.782)
Hotels, restaurants and bars	1.075 (0.699)	0.934 (0.731)	1.088 (0.889)	1.111 (0.845)
Transport, storage and communication	-0.168 (0.772)	0.268 (0.808)	-1.176 (1.259)	-0.777 (1.319)
Financial intermediation	1.176 (0.792)	0.221 (0.780)	-0.727 (1.047)	-0.703 (1.007)
Real estate, renting and business activities	-0.597 (0.655)	-0.424 (0.716)	1.601 (0.913)	1.741** (0.867)
Health and social work	-1.022 (0.776)	-0.869 (0.798)	0.910 (1.016)	0.945 (0.950)
Other community, social and personal activities	-0.297 (0.795)	0.046 (0.817)	1.083 (1.061)	1.441 (0.954)
Belgium	0.901 (0.641)	1.202 (1.033)	-0.895 (1.057)	-0.432 (0.951)
Denmark	0.932 (0.666)	1.419* (0.824)	-0.528 (1.062)	-0.461 (1.170)
Germany	1.586 (0.626)	1.539* (0.764)	0.221 (0.863)	0.055 (0.922)
Spain	1.480 (0.556)	1.182 (0.751)	-1.419 (1.067)	-2.070* (1.124)
Finland	0.312 (1.815)	0.341 (1.882)	-1.511 (1.036)	-1.846 (1.106)
Ireland	0.530 (0.699)	1.023 (0.954)	1.213 (1.427)	-1.223 (1.437)
Italy	1.530 (0.591)	1.816* (0.735)	-0.441 (0.856)	-0.522 (0.877)
The Netherlands	-0.120 (0.570)	0.125 (0.746)	0.505 (1.100)	0.562 (1.214)
Portugal	1.947 (0.811)	1.723 (1.012)	1.522 (1.845)	1.016 (1.853)
Sweden	0.398 (0.651)	0.821 (0.836)	0.703 (0.763)	0.894 (0.906)
United Kingdom	0.110 (0.533)	0.156 (0.696)	-0.365 (0.749)	-0.380 (0.781)
2003	-0.456 (0.373)	-0.724** (0.334)	-0.351 (0.492)	-0.405** (0.427)
Adjusted R ²	0.423	0.543	0.289	0.326
Observations	487	487	455	455

- Notes:
- i) Estimation method: Weighted OLS with constant included.
 - ii) ***, **, *, denote, respectively, significance at 1, 5, 10% level.
 - iii) Standard deviations of the coefficients are in parentheses and robust against any form of heteroskedasticity.
 - iv) Compliance costs and its relative burden are in logarithms. Zero observations on compliance costs have been excluded.

Table F-10 VAT compliance costs – un-weighted results

Dependent variable	Model 1	Model 2	Model 3	Model 4
	Compliance costs (1000 euros)	Compliance costs (1000 euros)	Compliance costs/sales	Compliance costs/sales
Company characteristics				
Small	0.464 (0.355)	0.458 (0.360)	-0.287 (0.415)	-0.289 (0.420)
Medium	0.707** (0.301)	0.749*** (0.297)	-1.214*** (0.456)	-1.212*** (0.458)
Large	1.718*** (0.289)	1.699*** (0.289)	-2.224*** (0.435)	-2.176*** (0.443)
Parent with subsidiary/branches/ permanent establishments in Home State	0.348 (0.232)	0.373 (0.231)	-0.685** (0.308)	-0.627** (0.307)
Parent with subsidiary/branches/ permanent establishments in other Member States	1.392*** (0.201)		-0.031 (0.258)	
<u>Domestic Companies without a subsidiary, branch or permanent establishment in other Member States:</u>				
2. Only foreign VAT activities without physical presence		-0.103 (0.424)		-0.424 (0.455)
3. Only VAT incurred on inputs abroad		-0.320 (0.226)		-0.599* (0.306)
4. Both foreign VAT activities without physical presence and VAT incurred on inputs abroad		-0.180 (0.448)		-0.264 (0.818)
<u>Companies with a subsidiary, branch or permanent establishment in other Member States:</u>				
5. No foreign VAT activities without physical presence and no VAT incurred on inputs abroad		0.754*** (0.271)		-0.284 (0.432)
6. Only foreign VAT activities without physical presence		1.471*** (0.435)		-0.011 (0.510)
7. Only VAT incurred on inputs abroad		0.859*** (0.368)		-0.295 (0.401)
8. Both foreign VAT activities without physical presence and VAT incurred on inputs abroad		2.429*** (0.331)		-0.234 (0.437)
Manufacturing	-0.636 (0.527)	-0.558 (0.601)	-0.366 (0.532)	-0.304 (0.588)
Electricity, Gas and water supply	-0.526 (0.754)	-0.350 (0.809)	-1.083 (0.822)	-1.131 (0.864)
Construction	-0.502 (0.579)	-0.467 (0.644)	-0.053 (0.657)	-0.097 (0.698)

Wholesale and retail trade	-0.600 (0.534)	-0.397 (0.610)	-1.339** (0.574)	-1.276** (0.625)
Hotels, restaurants and bars	-0.888 (0.580)	-0.662 (0.650)	-0.133 (0.646)	-0.128 (0.713)
Transport, storage and communication	-0.753 (0.570)	-0.574 (0.625)	-0.585 (.655)	-0.453 (0.705)
Financial intermediation	-0.731 (0.582)	-0.483 (0.651)	-1.583 (0.604)	-1.621** (0.673)
Real estate, renting and business activities	-1.188** (0.548)	-1.091* (0.623)	0.077 (0.589)	0.092 (0.645)
Health and social work	-1.313** (0.606)	-1.176* (0.672)	-1.290 (0.810)	-1.320 (0.886)
Other community, social and personal activities	-1.132* (0.651)	-0.966 (0.710)	-0.387 (0.602)	-0.383 (0.663)
Belgium	-0.616 (0.829)	-0.404 (0.874)	-0.6945 (0.972)	-0.709 (1.016)
Denmark	0.316 (0.380)	0.381 (0.381)	0.031 (0.458)	-0.051 (0.476)
Germany	0.226 (0.383)	0.202 (0.382)	0.623 (0.393)	-0.674* (0.413)
Spain	1.206** (0.579)	1.458*** (0.626)	0.247 (1.465)	0.192 (1.493)
Finland	-0.601 (0.501)	-0.604 (0.494)	-0.504 (0.491)	-0.620 (0.526)
Ireland	-0.321 (0.515)	-0.107 (0.534)	0.710 (0.855)	0.580 (0.858)
Italy	1.057** (0.471)	1.159** (0.469)	0.370 (0.551)	0.237 (0.581)
The Netherlands	0.402 (0.357)	0.460 (0.358)	0.515 (0.404)	0.468 (0.434)
Portugal	0.667 (0.483)	0.838 (0.481)	0.642 (0.573)	0.538 (0.583)
Sweden	-0.407 (0.547)	-0.297 (0.544)	0.482 (0.437)	0.445 (0.487)
United Kingdom	-0.190 (0.371)	-0.020 (0.366)	-0.038 (0.381)	-0.068 (0.416)
2003	-0.038 (0.239)	-0.013 (0.242)	0.068 (0.305)	0.043 (0.304)
Adjusted R ²	0.272	0.295	0.209	0.204
Observations	487	487	455	455

Table F-11 VAT compliance costs – subsidiaries abroad

	Model 2	Model 4
Dependent variable	Compliance costs (1000 euros)	Compliance costs/sales
Company characteristics		
Small	-0.006 (0.428)	-0.512 (0.619)
Medium	0.537 (0.539)	-2.301*** (0.754)
Large	0.816* (0.480)	-2.833*** (0.722)
Parent with subsidiary/branches/ permanent establishments in Home State	0.687 (0.390)	0.013 (0.450)
Subsidiaries in other Member States: 1-5	2.074*** (0.460)	1.951*** (0.700)
Subsidiaries in other Member States: 6-15	2.278*** (0.433)	0.137 (0.647)
Subsidiaries in other Member States: 16-50	3.104* (1.630)	-3.816* (2.196)
Subsidiaries in other Member States: >50	0.694 (0.695)	-1.249 (0.911)
2003	-0.457 (0.371)	-0.330 (0.492)
<i>Sectors (10)</i>	Yes***	Yes***
<i>Countries (11)</i>	Yes**	Yes*
Adjusted R ²	0.455	0.321
Observations	487	455

- Notes:
- i) Estimation method: Weighted OLS with constant included.
 - ii) ***, **, *, denote, respectively, significance at 1, 5, 10% level.
 - iii) Standard deviations of the coefficients are in parentheses and robust against any form of heteroskedasticity.
 - iv) Compliance costs and its relative burden are in logarithms. Hence, zero observations on compliance costs are excluded.

Table F-12 Regression Sample Statistics

Dependent variable	Absolute total compliance costs	Relative total compliance costs	Absolute company taxation compliance costs	Relative Company Taxation Compliance Costs	Absolute VAT Compliance Costs	Relative VAT Compliance Costs
(logarithms)	3.667 (2.283)	-6.129 (2.491)	3.024 (2.324)	-6.935 (2.382)	2.707 (2.226)	-7.272 (2.611)
Micro	0.178	0.176	0.170	0.164	0.156	0.156
Small	0.205	0.204	0.195	0.191	0.193	0.191
Medium	0.241	0.238	0.241	0.241	0.248	0.246
Large	0.376	0.382	0.394	0.403	0.402	0.409
No subsidiaries , branches or permanent establishments	0.283	0.281	0.264	0.259	0.263	0.257
Only subsidiaries, branches or permanent establishments in the Home State	0.437	0.433	0.449	0.450	0.452	0.450
Only subsidiaries, branches or permanent establishments in other Member States	0.016	0.017	0.013	0.014	0.012	0.013
Subsidiaries , branches or permanent establishments in both the Home State and other Member States	0.264	0.270	0.275	0.281	0.273	0.279
Subsidiaries in other Member States:	0.159	0.170	0.161	0.173	0.160	0.171

Austria	0.045	0.047	0.050	0.052	0.049	0.051
Belgium	0.017	0.019	0.019	0.020	0.014	0.015
Denmark	0.206	0.192	0.220	0.203	0.205	0.191
Germany	0.108	0.103	0.105	0.101	0.109	0.103
Greece	0.003	0.004	-	-	-	-
Spain	0.014	0.015	0.013	0.014	0.012	0.013
Finland	0.066	0.067	0.073	0.074	0.072	0.073
Ireland	0.035	0.036	0.031	0.032	0.031	0.031
Italy	0.075	0.077	0.065	0.068	0.068	0.070
The Netherlands	0.164	0.165	0.136	0.137	0.162	0.163
Portugal	0.058	0.062	0.057	0.061	0.055	0.059
Sweden	0.028	0.028	0.029	0.029	0.029	0.029
United Kingdom	0.178	0.185	0.201	0.209	0.193	0.202
1. Pure domestic company					0.524	0.524
2. Only foreign VAT activities without physical presence					0.023	0.023
3. Only VAT incurred on inputs abroad					0.146	0.146
4. Both foreign VAT activities without physical presence and VAT incurred on inputs abroad					0.023	0.023

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